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TEMPORARY NATIONAL ECONOMIC COMMITTEE

A STUDY MADE FOR THE TEMPORARY NATIONAL ECONOMIC COMMITTEE, SEVENTY-SIXTH CONGRESS, THIRD SESSION, PURSUANT TO PUBLIC RESOLUTION NO. 113 (SEVENTY-FIFTH CONGRESS), AUTHORIZING AND DIRECTING A SELECT COMMITTEE TO MAKE A FULL AND COMPLETE STUDY AND INVESTIGATION WITH RESPECT TO THE CONCENTRATION OF ECONOMIC POWER IN, AND FINANCIAL CONTROL OVER, PRODUCTION AND DISTRIBUTION OF GOODS AND SERVICES

MONOGRAPH No. 11-14

BUREAUCRACY AND TRUSTEESHIP IN LARGE CORPORATIONS

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Monograph No. 11

BUREAUCRACY AND TRUSTEESHIP IN LARGE CORPORATIONS

MARSHALL E. DIMOCK and HOWARD K. HYDE

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The Temporary National Economic Committee is greatly indebted to these authors for their contribution to the literature of the subject under review.

The status of the materials in this volume is precisely the same as that of other carefully prepared testimony when given by individual witnesses; it is information submitted for Committee deliberation. No matter what the official capacity of the witness or author may be, the publication of his testimony, report, or monograph by the Committee in no way signifies nor implies assent to, or approval of, any of the facts, opinions, or recommendations, nor acceptance thereof in whole or in part by the members of the Temporary National Economic Committee, individually or collectively. Sole and undivided responsibility for every statement in such testimony, reports, or monographs rests entirely upon the respective authors.

(Signed) JOSEPH C. O'MAHONEY,
Chairman, Temporary National Economic Committee.

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LETTER OF TRANSMITTAL

Hon. JOSEPH C. O'MAHONEY,
Chairman, Temporary National Economic Committee,
Washington, D. C.

MY DEAR SENATOR O'MAHONEY: I transmit herewith a monograph written under the auspices of the Temporary National Economic Committee on the subject of Bureaucracy and Trusteeship in Large Corporations.

Beginning with a summary of the available information on diffusion of corporate ownership and the separation of ownership and control, it plunges into an anatomical study of bureaucracy. In dealing with the structural and personnel problems inherent in size it discusses the managerial correctives employed and recommends some that might secure and enforce greater trusteeship in business management. In particular, it emphasizes the salutary effect of full transparency of business operations.

This study would have been impossible without the generous cooperation of the United States Department of Labor and the consent of those in charge of the Public Administration Fund at the University of Chicago and the Rockefeller Foundation that a portion of the results of a much larger study on corporate administration now being made at the University of Chicago be made available to the committee.

To give full acknowledgment to all of those in business and in government who have given of their time and knowledge to the preparation and review of various portions of this monograph would unreasonably tax the patience of the reader. But it would be definitely remiss to omit an expression of gratitude to the reviewers who have gone over this document in its entirety: Mr. Archibald R. Graustein, formerly president of the International Paper & Power Corporation; Dr. Lloyd G. Reynolds, of the economics staff at Johns Hopkins University; and Dr. Edward S. Mason, professor of economics, Harvard University.

Respectfully submitted.

THEODORE J. KREPS,
Economic Adviser

AUGUST 16, 1940.

PREFACE

Much of the material on which this study is based was secured during the course of a research which the authors began at the University of Chicago several years ago. This larger inquiry has not been completed nor the results published.

The University of Chicago study was financed by the Public Administration Fund of that institution, which in turn was assisted by the Rockefeller Foundation. The present monograph was not contemplated when the original research was planned and the materials gathered. When the Temporary National Economic Committee learned of the existence of this inquiry, however, they asked for a monograph on bureaucracy and trusteeship in large corporations. Those responsible for the university research fund kindly acceded to the request.

The University of Chicago study has been concerned with the methods which large corporations have found efficacious in dealing with the complex problems of organization and personnel with which they are beset. Power relationships exist. Bureaucracy is seemingly inherent. To what extent can forethought, philosophy, and Yankee ingenuity counteract the inflexibilities incident to large size? In what respects are the manifestations of and remedies for bureaucracy alike in business and in government, and in what ways are they different? It is hoped that some of the basic considerations applicable to both will emerge as a result of the larger study.

The present monograph, as we have said, draws upon only part of the materials. In addition to published studies and other written data we have made extensive first-hand observations in selected corporations. Approximately 30 corporations were so chosen and 250 executives, high and low, were interviewed. Some were consulted several times and use was made of the prolonged interview. Four representative corporations were chosen for special study. The American Telephone & Telegraph Co. was rather intensively dealt with, for it presents much of interest in management policy and technique.

For the most part, the names of corporations and officials will not be divulged in the pages which follow, for no good purpose would be served in so doing and the authors would not want to quote officials by name without their express permission. Quotations are drawn from interviews, however, and for this assistance, even though not acknowledged in footnotes, the authors are grateful.

MARSHALL E. DIMOCK.
HOWARD K. HYDE.

JUNE 15, 1940.

PART I

THE NATURE AND SCOPE OF BIG BUSINESS

CHAPTER I

THE DEVELOPMENT OF GIANT CORPORATIONS

When large machines superseded the craftsman with his kit of tools, the owner of machines became the master of the Nation's industry. As the number of stockholders in the modern corporation constantly multiplied, however, so that at length no one person owned a large percentage of the business, the manager of the concern tended to replace the owner as the wielder of actual power. Professional managers, owning none or but a small amount of stock themselves—this is the pattern of business which has become prevalent today.

It has always been an assumption of civilized communities that with power there goes a corresponding responsibility. Usually this responsibility has to be enforced; and at least the many, if they are wise, will attempt to set limits, establish rules, and provide instruments of coercion, lest the few be tempted to abuse their power. This is the history of all government, and it is peculiarly the essence of the democratic form of government, whether that government be political or industrial.

When business is small the problems of control and management are usually simple. The individual who has the money and the market also runs the business. Quite a different situation arises, however, when one group of people furnishes the capital and another runs the business for it. Then, potentially at least, both owners and laborers are dispossessed, as earlier the financier gained the ascendancy over the craftsman. Under modern conditions existing in the corporate form of enterprise we have what has come to be appropriately called management control. The owners own, but they find it difficult to exercise real authority. The managers do not own, but actually exercise the power which determines the success or failure of the enterprise.

The modern semipublic corporation is obviously a trusteeship, a legal-administrative relationship in which the owners, theoretically at least, entrust the managers with power to carry on the business for them so long as their mandate is complied with and the results are generally satisfactory. What are the implications of trusteeship, not only for the trustees but also for capital, labor, and the public? How, if necessary, can accountability be enforced and sanctions imposed? What are the consequences of control without ownership for the government of business and for political democracy itself? A familiar problem to the student of the state—not so often explored by students of the business order.

A second consequence of machine technology and corporate finance is the very complexity of giant corporations. The vaster they become the more difficult are the structural problems of organization, coordination, and control, and the human problems of incentive and leadership. Large corporations, like other large human enterprises, are bureaucratic. They tend to live by fixed rules rather than acumen,

by the meshing of many component parts rather than the quick decision of an entrepreneur. Organization grows in importance as size increases and trusteeship gains ascendancy. And like other large organisms, the larger the modern corporation becomes, the more it tends to move slowly, adapt itself with increasing difficulty, be increasingly concerned with its inner rules and procedures. Hence, it stands in danger of losing that flexibility of price adjustment and resiliency of managerial outlook which is the most valuable social asset of free competition. Can it be prevented? Are there discoverable, reliable offsets to the undesirable aspects of bureaucracy? First we must know what we mean by bureaucracy and the causes of its objectionable manifestations.

This is obviously the task of the student of institutional structure and functioning, the student of government. His job and that of the economist are interrelated. If we knew for sure whether bureaucracy is inherent in large corporations, how objectionable, if at all, some of its manifestations are, and how possible it is to provide correctives, then we could act with greater assurance on the questions of enforced competition and small versus large units of business enterprise.

What is the situation today? Fifty years ago approximately half of the gainfully employed persons in the United States were engaged in agriculture. Now, however, agriculture claims only about a fifth of the gainfully occupied, while industry [1] has become the employer of over half this group.[2] Industry, moreover, is characterized by its predominantly urban location and by a seemingly inherent tendency to coalesce into progressively larger units.

The concept of big business is not new to the American vocabulary. In the latter part of the last century the trusts provided potent political issues and the popular fear of bigness found expression in the enactment of the anti-trust laws. The passage of these laws seemed to alleviate in part the current apprehensions without, however, effectively blocking the growth of great enterprises.[3] We need not here go into the legal, political, and economic causes of this nonfulfillment of apparent intentions; it will suffice to point out the growth which has occurred.

In 1909 the 200 largest nonfinancial corporations held approximately a third of the assets of all such corporations.[4] By 1930 over half of the assets were so owned. In 1933 the physical assets of the 200 giants constituted about 60 percent of all those held by nonfinancial corporations, about half of the total industrial wealth, or about a fifth of the total national wealth. Expressed in monetary terms, these few corporations owned physical assets aggregating some 64 billions of dollars.[5]

It should be noted that the roster of the 200 giants varies from year to year. These changes, however, indicate the differences in the

[1] Including the census groups of extraction of minerals, manufacturing, and mechanical industries, transportation and communication, and trade.

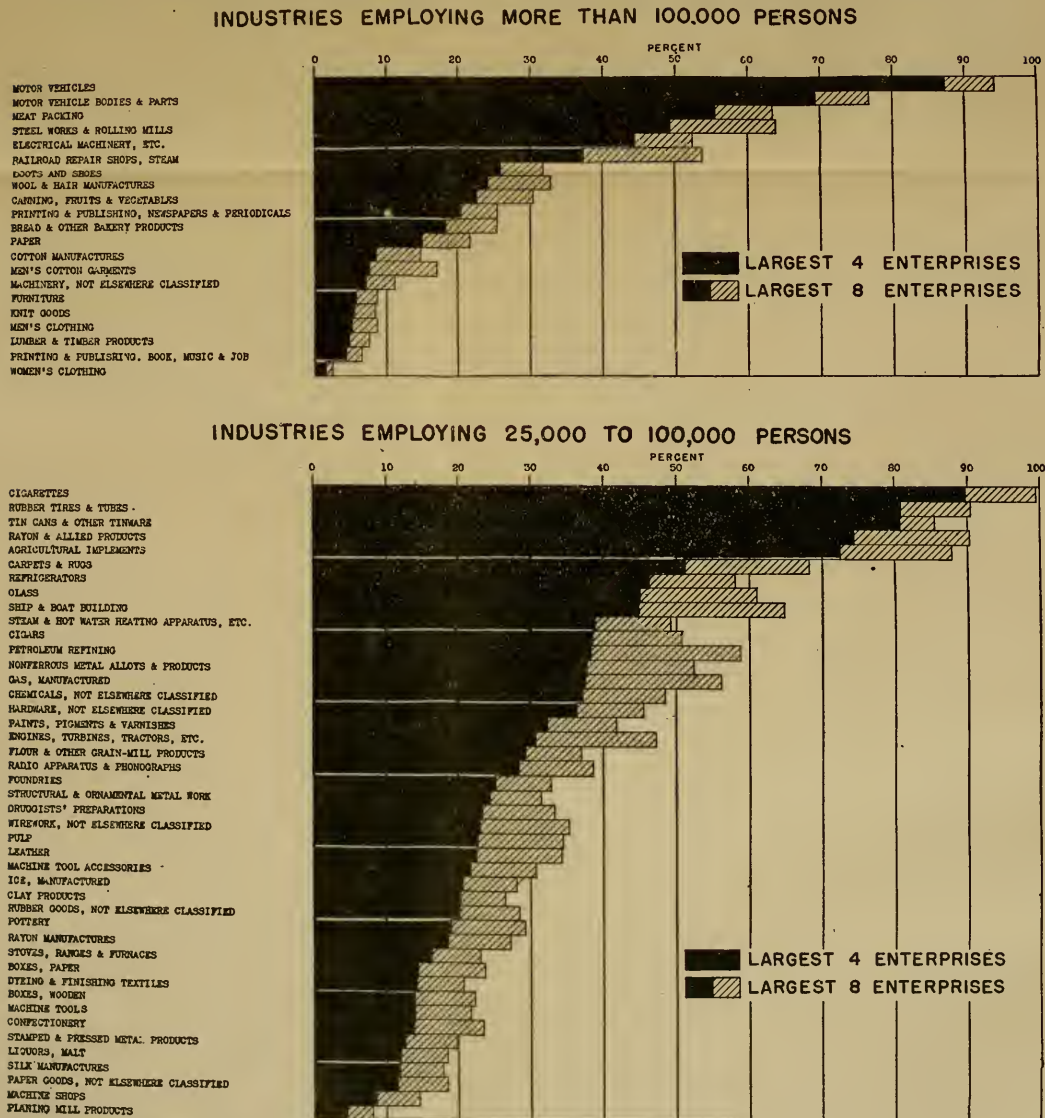
[2] U. S. Department of Commerce, Abstract of the Fifteenth Census of the United States (Washington: Government Printing Office, 1933), p. 305.

[3] In fact, Thurman Arnold argues that the antitrust laws actually assisted in the growth of big business. See his Folklore of Capitalism (New Haven: Yale University Press, 1937), ch. IX.

[4] Financial and nonfinancial corporations are not strictly comparable. For one thing, the assets of the former are constituted largely of claims on the latter.

[5] National Resources Committee, The Structure of the American Economy, Part I (Washington: Government Printing Office, 1939), pp. 106–107. This report was prepared under the direction of G.C. Means. See also: A. A. Berle and G. C. Means, The Modern Corporation and Private Property (New York: Macmillan, 1932), ch. III; the testimony of Willard Thorp before the Temporary National Economic Committee, which is summarized in the committee's preliminary report on the Investigation of Concentration of Economic Power, 76th Cong., 1st sess., S. Doc. No. 95, 1939, p. 6; and the Twentieth Century Fund's Big Business: Its Growth and Its Place (New York: Twentieth Century Fund, 1937).

Chart I.—Concentration, Measured by Value of Products, in Manufacturing Industries 1935[1]



[1] From National Resources Committee, The Structure of the American Economy, Part I (Washington: Government Printing Office, 1939), p. 112

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rate of growth among particular corporations and the mortality of the giants. They do not necessarily affect the degree and growth of concentration which exists for industry as a whole. It is this phase of the problem in which we are primarily interested.

The concentration of business into large units has not taken place uniformly throughout the economic structure. Some industries have a much greater tendency toward bigness than others. For example, 90 percent of the Nation's railroad mileage is operated by corporations on the list of the 200 giants; 80 percent of the electric-power production, practically all the telephone and telegraph service and a large part of the metropolitan rapid-transit systems may also be so classified.[6] In the industrial group the picture is spotty. Some industries show a high degree of concentration, while others are at the opposite extreme. The over-all role of the large corporation in manufacturing may be indicated thus:

With size measured by employment: One hundred companies employed 20.7 percent of all the manpower engaged in manufacturing;

With size measured by value added by manufacturing: One hundred companies contributed 24.7 percent of all the value added in manufacturing activity;

With size measured by value of product: One hundred companies accounted for 32.4 percent of the value of products reported by all manufacturing plants.[7]

An indication of concentration in particular manufacturing industries is given in chart I, which includes data for all census industries employing more than 25,000 persons. The degree of concentration in four industrial categories is indicated in table I.

TABLE I.—*Concentration in 4 industrial categories, 1933* [1]

Proportion of corporate assets in 4 industrial categories controlled by largest corporations in these categories	1933: Total assets less taxable investments (less depreciation)	1933: Land, buildings, and equipment (less depreciation)
	Percent	*Percent*
75 largest manufacturing corporations	40.2	45.5
45 largest transportation corporations	91.7	91.6
40 largest public utility corporations	80.4	81.2
25 largest "other" nonfinancial corporations	14.8	17.4

[1] From National Resources Committee, The Structure of the American Economy, Part I (Washington: Government Printing Office, 1939), p. 106.

In the field of trade, the 10 mail-order houses, retail chains, and department stores which are on the list of the 200 giants account for about 8 percent of the Nation's retail sales. It is apparent that the great bulk of this part of business is carried on by small units.

There is somewhat more concentration in the financial field. The 30 largest banks "together hold 34.3 percent of the banking assets of the country outside of the Federal Reserve banks while * * * 17 life-insurance companies account for over 81.5 percent of the assets of all life-insurance companies." [8]

Several occupational fields are dominated by small enterprise. Foremost among these is, of course, agriculture. In 1935 the "7,000,000 farm units each engaging the activities of only one to five persons accounted for well over half of the total number of producing

[6] It should be noted that these industries fall in the group which is commonly called natural monopolies.
[7] National Resources Committee, op. cit., p. 102.
[8] Ibid., p. 103.

units in the country and together they accounted for 97 percent of the persons engaged in agriculture." [9] Nonutility services (except for some branches such as motion pictures and education), retail trade, and construction are characterized by small enterprise. For example, retail stores with annual sales of less than $30,000 and usually employing one or two persons accounted for 30 percent of total retail sales in 1935. Construction presents a similar picture.

The general view on concentration in American industry may be stated in summary terms: "Altogether, little more than a third of the Nation's economic activity is carried on by producing units engaging the activity of one to five persons. An almost equal proportion was carried on by a few hundred very large administrative units." [10]

Concentration, however, is carried beyond that attained by the formal organization of giant corporations and their majority-controlled subsidiaries. Several less formal methods exist whereby the corporate giants are loosely bound together in groups of varying size and solidarity. Foremost among these methods are interlocking directorates, services of large financial institutions, intercorporate stockholdings, and important stock ownership in several corporations by an individual or group of individuals, various trade and general business associations, and sometimes a tacit acceptance of noncompetition.

The existence of interlocking directorships is not conclusive proof that the companies involved work in close harmony. Some directors in reality have little to say about management, either because they are relatively inactive, or because they are members of the minority, or, perhaps most common of all, because the officers of the particular companies run their enterprises without substantial assistance from the boards. Nevertheless, many directors are influential and in any case there can be little doubt that interlockings at least contribute substantially to the so-called climate of opinion within which policies are determined. Moreover, the majority of those who hold the most directorships among the largest corporations also have active positions in at least one of the companies they serve. It is possible that "such men are likely to take a responsible share in the development of policy in any corporation in which they hold a responsible position." [11]

TABLE II.—*Number of directors and their holdings of directorships in the 200 largest nonfinancial and 50 largest financial corporations, 1935* [1]

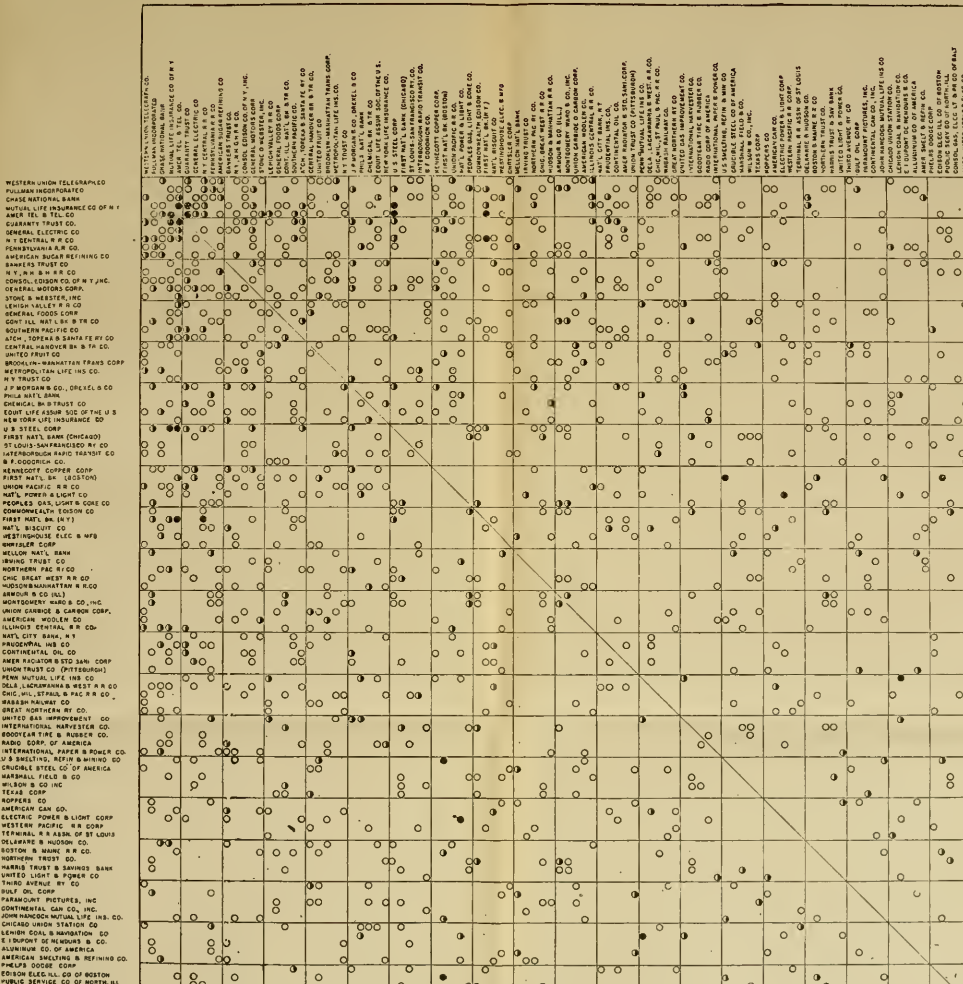
Number of directorships held by a single indivudal	Total number of directors	Total number of directorships held	Cumulative number	
			Directors	Directorships
9	1	9	1	9
8	3	24	4	33
7	6	42	10	75
6	6	36	16	111
5	19	95	35	206
4	48	192	83	398
3	102	306	185	704
2	303	606	488	1,310
1	2,234	2,234	2,722	3,544
Total	2,722	3,544		

[1] From National Resources Committee, The Structure of the American Economy, Part I (Washington: Government Printing Office, 1939), p. 158.

[9] Ibid., p. 103.
[10] Ibid., p. 104.
[11] Ibid., p. 158.

Chart II.—Interlocking Directorates Among 100 Large Corporations, 1935

ARRANGED IN ORDER OF NUMBER OF INTERLOCKS[1]



LEGEND

○ 1 DIRECTOR IN COMMON
◑ 2-3 DIRECTORS IN COMMON
● 4 OR MORE DIRECTORS IN COMMON

FOR CONVENIENCE IN READING THE CHART, INTERLOCKS ARE SHOWN TWICE, ONCE IN THE UPPER AND ONCE IN THE LOWER HALF OF THE CHART

[1] From National Resources Committee, The Structure of the American Economy, Part I (Washington: Government Printing Office, 1939), p. 158A.

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Of the 3,544 directorships on the boards of the 200 largest nonfinancial and 50 largest financial corporations in 1935, 400 men held approximately a third. The distribution of all of the directorships in these corporations is presented in table II.[12] As might be expected, the extent of interlocking varies widely among the big companies. Twenty-five of the companies had no interlocks with others on the list of 250, but 151, representing nearly three-fourths of the assets, interlocked with 3 or more others and 10 interlocked with 26 or more. The 100 companies with the most interlocks are ranked in order in chart II. It would be too great a strain on human nature to expect that individuals holding more than 1 directorship would refrain from carrying the interests of 1 company over into their deliberations on the affairs of other corporations.

Minority stock ownership is another tie that binds the corporate group together. The minority stock may be held by an individual or group of individuals, as illustrated by the Rockefeller group of oil companies, or it may be held by another corporation:

> In the case of at least 30 of the 250 large corporations, 10 percent or more [but less than 50 percent] of the voting power derived from stock ownership was held directly or indirectly by another corporation in the group or by one of the 9 financial or holding companies not included in the list of 250 corporations but clearly part of the corporate community. In all but 1 of these cases, corporate stockholders were the only stockholders with 10 percent or more of the voting power.[13]

Since 10 to 20 percent of the voting power is commonly spoken of as constituting a so-called working control it can readily be seen that overlapping minority holdings significantly contribute to concentration in American industry.

The services of large financial institutions constitute a third informal tie. The influence of the bankers has doubtless often been overestimated but it cannot help being real. Most of the issuing of new securities by the largest corporations is handled by a relatively small number of financial companies. For example, in 1935, 175 of the largest 200 nonfinancial companies issued new securities. Since 10 firms initiated 56 percent of all corporate underwriting,[14] it is probable that the securities of the giants were handled by a correspondingly small number of investment houses.

Interest on the part of financial companies in the managerial affairs of other large corporations, however, does not stem only from the process of floating new securities. The companies are also a significant group of investors themselves. In 1935, for example, financial institutions owned about a fourth of all corporate bonds outstanding.[15] In addition, there is a large but unestimated amount of loans and credits of a more short-term nature advanced to corporations by financial concerns. These lending and investing companies are interested in management and corporate policy not only when making the original advances of credit but also when the recipients run into difficulties of repayment.

In corporate reorganizations various protective and other committees play a key part. The groups which are influential in con-

[12] This table presents only the directorships held on the boards of the 250 giants. It does not show the numerous directorships held by these men on the boards of lesser companies.

[13] Ibid., pp. 158–159.

[14] Ibid., p. 159.

[15] Ibid., pp. 159–160, citing Twentieth Century Fund, Debts and Recovery (New York: Twentieth Century Fund, 1938), p. 287.

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trolling these committees stand to gain most in the subsequent reorganization. After a comprehensive investigation of such committees the Securities and Exchange Commission concluded that "by and large, control over committees has been in the hands of the management and the bankers * * *. The bankers * * * to a great extent, have been the spokesmen and strategists for the management in reorganizations." [16]

The suppliers of credit can ill afford not to be concerned with corporate policies which can have such an important effect in establishing the quality of an investment. The inevitable result is thus a further linking of the nonfinancial giants through the medium of a relatively small number of financial corporations. It should be pointed out, however, that this linking does not necessarily mean that financial institutions control the nonfinancial companies involved. In the United States the case of a financial corporation being under the influence of an industrial group is quite as likely to occur as is the reverse. The process of linking does, however, result in a concentration of industry. Whether the top control is by financial or nonfinancial institutions need not concern us at the moment.

TABLE III.—*8 interest groups and their assets, 1935* [1]

[Millions of dollars]

	Morgan First National	Rockefeller	Kuhn, Loeb	Mellon	Du-Pont	Chicago	Cleveland	Boston	Total assets
Industrials	3,920	4,262	0	1,648	2,232	858	1,066	425	14,411
Rails	9,678	0	9,963	153	0	0	0	0	19,794
Banks	4,421	2,351	548	672	396	2,595	338	740	12,061
Utilities	12,191	0	342	859	0	813	0	554	14,759
Total assets	30,210	6,613	10,853	3,332	2,628	4,266	1,404	1,719	61,025

[1] From National Resources Committee, The Structure of the American Economy, part I (Washington: Government Printing Office, 1939), p. 161.

Using these and other criteria of corporate interrelationship, Gardiner Means and his associates have arranged 106 of 250 giants into 8 interest groups which include about 60 percent of the assets of all these companies.[17] The groups and their assets are given in table III. A tabular view of the interlocking directorates of the corporations in these groups is presented in chart III.

Two of the classifications indicated here receive their names from financial institutions. The Morgan-First National group is so designated because much of the interrelation of the corporations which are included is brought about through these two closely identified concerns. As a group it contains representatives of most of the major industries in the Nation. The Kuhn, Loeb unit is composed primarily of railroads whose financing has been handled for many years by this firm.

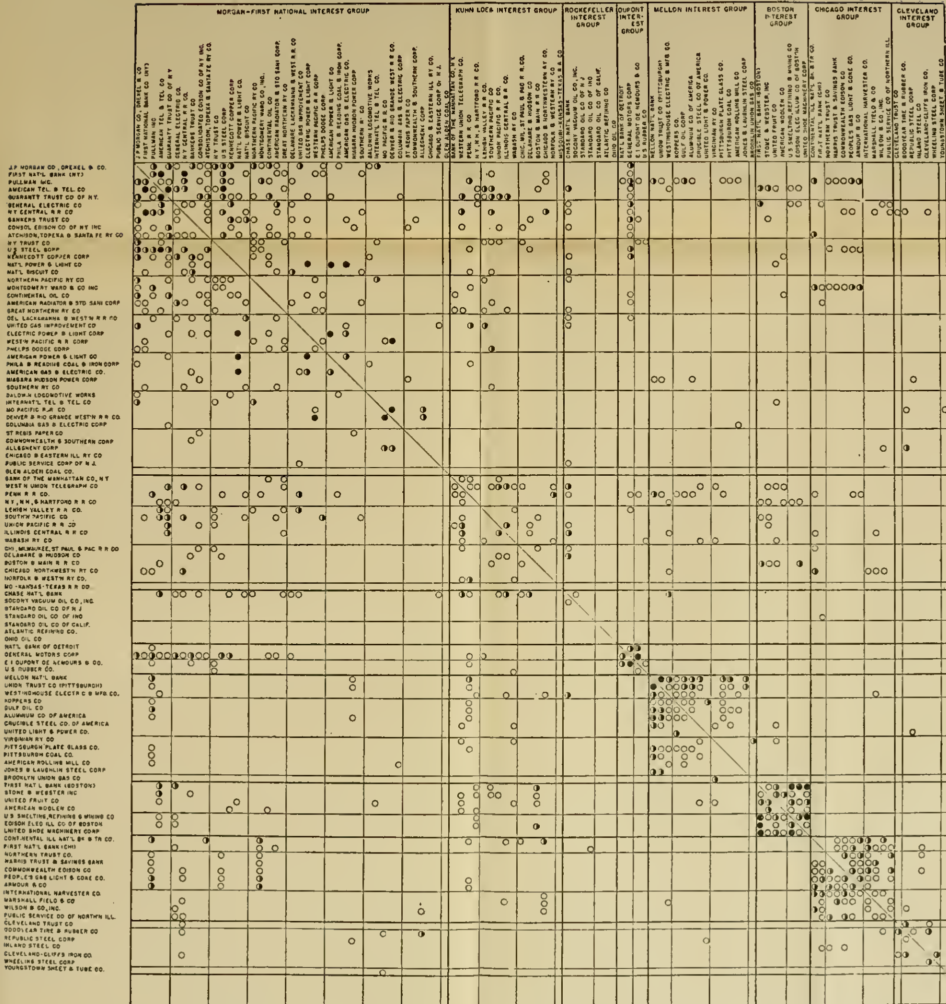
Three groups coalesce around particular families. That of Rockefeller includes six oil companies, which are successors to the old Standard Oil Co., and one bank. Rockefeller interests have important minority holdings in all these oil companies—usually the only sub-

[16] Securities and Exchange Commission, The Work Activities, Personnel and Functions of Protective and Reorganization Committees, Part I (Washington: Government Printing Office, 1937), p. 342.

[17] National Resources Committee, op. cit., pp. 160–163, 306–317.

CHART III.—INTERLOCKING DIRECTORATES AMONG 106 LARGE CORPORATIONS, 1935

ARRANGED ACCORDING TO INTEREST GROUPINGS[1]



LEGEND

- ○ 1 DIRECTOR IN COMMON.
- ◑ 2–3 DIRECTORS IN COMMON.
- ● 4 OR MORE DIRECTORS IN COMMON.

[1] From National Resources Committee, The Structure of the American Economy, Part I (Washington: Government Printing Office, 1939), p. 162A.

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stantial stock interest in each case. Together the oil concerns control over half the assets of their industry. The Mellon family has a number of companies from different types of industries, centering largely in and around Pittsburgh, assigned to it. In about half of these companies, Mellon interests appear to own a majority of the outstanding stock. Four companies are assigned to the Du Pont family, chiefly on the basis of large minority stock holdings.

The other three groups appear to gain their cohesiveness largely because of the location of the companies involved. There is, however, a great deal of interrelationship among the members of the particular groups. The corporate clusters are named for their respective geographical locations—Boston, Chicago, and Cleveland—and their rather high concentration of interlocking directorships is shown in chart III.

One further method of intercorporate concentration should be noted—that of the trade and business associations. In 1937 there were over 2,400 national or interstate associations,[18] which were of varying significance in the national economy. The national associations of steel companies, manufacturers, bankers, railroads, and electric utilities are largely dominated by big corporations and thus constitute an extension of their influence. Some of the associations of retailers, on the other hand, are composed primarily of small businesses.

To a large extent these associations exert their influence through affecting the climate of opinion within which policies are formed and in serving as the spokesmen for their members on public questions. One, the United States Chamber of Commerce, speaks for a very broad group. Some go further than this. The National Retail Trades Association, for example, has conducted a rather complete strike-breaking service.[19] Others, such as the cement association, through various means provide the medium for price uniformity. Thus, although the methods and effectiveness of the associations vary, there can be little doubt that they contribute substantially to concentration of policy formation and determination of methods in American industry.

[18] Ibid., p. 163.

[19] Ibid., p. 165, citing hearings before a subcommittee of the Committee on Education and Labor (the La Follette committee), U. S. Senate, 74th Cong., S. Res. 266, part 3, pp. 809 ff.

CHAPTER II

THE DIFFUSION OF OWNERSHIP

Big business is peculiarly dependent upon the corporate form for its metamorphosis into the modern giants. This creature of the state not only presents its owners with a welcome limit on their liability but opens up the way for the phenomenal growth which we have noted. The divisibility of ownership which arises from the device of stock enables the shares to become market commodities within the reach of multitudes.

With very rare exceptions, the corporate giants have grown faster then their original owners were able or willing to furnish the necessary capital. Even Henry Ford, it should be remembered, financed himself through a critical period by shipping automobiles to his dealers in excess of their orders and billing them for the shipments. Durant was unable to keep control of General Motors because of the demands for capital beyond his resources.[1] Alexander Bell and his associates soon lost control of the telephone company, which they founded, because they had to enlist outside capital, the suppliers of which demanded successive increases in control.[2] Thus the process has continued. Each substantial expansion typically requires an additional market for securities. Sometimes, of course, profits are large enough to finance expansion, at least for a time; or the original backers of the enterprise may have sufficient resources to keep it a closely held corporation. Characteristically, however, the corporate giants have a widely dispersed group of owners; and this is due, in part at least, to the large amounts of capital which are required.

In some cases wide dispersion of stock has been actively fostered by management.[3] The purposes involved have been several: the provision of a broad market for subsequent issues of securities, the spreading of interest in the particular company to a large number of local individuals, and the gaining of a relative increase in the control powers by management with a minimum of investment.

It is not surprising that no one investor has the billions of dollars which have gone into the capital structure of such giants as the American Telephone & Telegraph Co., the Pennsylvania Railroad, or the United States Steel Corporation. But one might not suspect the extent to which dispersion of ownership has taken place in these companies. In each of these cases the principal individual stockholder has held less than 1 percent of the outstanding stock.

The more generalized picture may be drawn from two standpoints: that of the number of stockholders of given corporations and that of

[1] Arthur Pound, The Turning Wheel (New York: Doubleday, Doran & Co., 1934), chs. VIII and XIII.
[2] Federal Communications Commission, Investigation of the Telephone Industry in the United States (Washington: Government Printing Office, 1939), pp. 83–84.
[3] See, for example, the activities of the Bell Telephone Securities Co., Federal Communications Commission, Investigation of the Telephone Industry in the United States (Washington: Government Printing Office, 1939), pp. 14–15.

the degree of concentration of stockholdings in the hands of one or a few persons. Of the 200 corporate giants which they examined, Berle and Means were able to obtain the size of the stockholder lists of 144 companies. These lists "revealed the fact that only 20, representing less than 5 percent of the assets of the 144 companies each had less than 5,000 stockholders, while as many as 71 companies had over 20,000. More than half the assets represented belonged to companies with 50,000 stockholders or more." [4] A classification of these companies is indicated in table IV.

TABLE IV.—*144 out of 200 largest companies distributed according to number of stockholders* [1]

	Railroads	Public utilities	Industrials	Total
Under 5,000	10	5	5	20
5,000 to 19,999	16	11	26	53
20,000 to 49,999	8	5	26	39
50,000 to 99,999	3	10	9	22
100,000 to 199,999	1	3	3	7
200,000 to 500,000	----------	3	----------	3
Total	38	37	69	144

[1] From A. A. Berle and G. C. Means, The Modern Corporation and Private Property (New York: Macmillan, 1932), p. 50.

While such a classification of company stockholders indicates the level of public participation which has been reached, it does not clearly show the degree to which concentration of ownership has ebbed. Berle and Means found that among their list of 200 corporations "only 11 percent of the companies and 6 percent of their wealth involved control by a group of individuals owning half or more of the stock interest outstanding." [5] A more recent study [6] indicates dispersion of ownership of a like magnitude. Using a summary report of the Securities and Exchange Commission,[7] plus other sources, Gordon classified 155 corporations of the Berle and Means selection of 200 according to the concentration of stockholdings. Of the 45 which were excluded, primarily for lack of data, 16 were not listed on any exchange and hence were probably closely held. The combined holdings, weighted according to voting power, of all officers, directors, and important outside interests are indicated in table V, together with the number of companies which fell in the various concentration classifications. This indicates that in approximately half of these companies the combined holdings of all members of the management and other important stockholders total only about 5 percent, while in no more than 15 cases did such total holdings constitute a majority of the potential votes. If we add the 16 companies on which data was not available, we get 31 of 171 giant corporations as members of that rather select group which have a voting majority of their stock held by a fairly small number of persons. Since these are combined figures, and since in a large proportion of the cases the

[4] Op. cit., p. 49.
[5] Ibid., p. 114.
[6] Robert A. Gordon, "Ownership by Management and Control Groups in the Large Corporation", Quarterly Journal of Economics, LII (May 1938), pp. 367–400.
[7] Securities and Exchange Commission, Official Summary of Holdings of Officers, Directors, and Principal Stockholders (Washington: Government Printing Office, 1936). This gives holdings as of December 31, 1935.

outside stockholders are other corporations,[8] it is obvious that the holdings of any individual stockholder are considerably less than is here indicated for his particular group.

It is frequently supposed that the management, including the directors, of large corporations own substantial blocks of stock in their own companies. Then, even though outside stockholders may be widely dispersed, they would be protected through the identity of their interests with those of the management. To an examination of the extent of the holdings of management we may now turn.

TABLE V.—*Concentration of control through stockholdings of 155 large corporations* [1]

Proportion of voting strength held by management and important outside groups:	*Number of companies*	Proportion of voting strength held by management and important outside groups—Continued	*Number of companies*
0 to 5 percent	73	35 to 40 percent	6
5 to 10 percent	13	40 to 45 percent	5
10 to 15 percent	11	45 to 50 percent	5
15 to 20 percent	8	50 percent and over	15
20 to 25 percent	8		
25 to 30 percent	5	Total	155
30 to 35 percent	6	Median	5.40

[1] Source: Robert A. Gordon, "Ownership by Management and Control Groups in the Large Corporations," Quarterly Journal of Economics, LII (May 1938), p. 381.

Gordon has classified management holdings in 155 giant companies according to industrial and asset groups. Parts of his findings are reproduced in tables VI and VII. These tables indicate that stock ownership on the part of officers and even of officers and directors combined is virtually nonexistent in a large section of our economy. In half of the 36 railroads examined, the officers held not more than four-hundredths of 1 percent (the median) of the voting power. The corresponding percentages for public utilities and industrials are 0.17 and 1.38, respectively. For all of the 155 companies combined, the proportion of voting stock held by the officers was only four-tenths of 1 percent. The addition of the holdings of nonofficer directors to those of the officers of course increases the percentages, but they still remain small. For the railroad group, in half of the cases the officers and directors own no more than 0.58 percent; the public-utility and industrial groups follow with 1.18 and 3.60 percent, respectively. The combined holdings of both officers and directors did not total more than 1.74 percent for half of the complete list of 155 corporations. In each of these business groups and for all of the corporations combined, it is thus apparent that in the typical large corporation management holdings are comparatively insignificant when expressed in relative terms.

Among the business giants there does not seem to be a clear-cut inverse relationship between the size of particular companies and the proportionate stockholdings of management. Table VII demonstrates this in a tabular view of 155 companies, showing the stockholdings of management in different asset classifications. There appears to be some inverse relationship in the industrial classification, but it is quite rough, while it is almost completely absent in the railroad

[8] "There is a marked absence of large outside holdings by individuals or families among the railroads and utilities; the outside holders are almost always other railroad and utility companies. Such intercorporate ownership is also found in the industrial field, but to a much less marked extent."—Gordon, op. cit., p. 397. For a list of intercorporate holdings of more than 10 percent among the large companies, see National Resources Committee, op. cit., p. 160.

and public utility fields. Thus throughout the asset scale from 50 million to 4 billion dollars the holdings of management are on the whole relatively small.[9]

TABLE VI.—*Distribution of 155 large corporations according to the proportion of voting stock owned by management, by industrial classes, Dec. 31, 1935* [1]

Proportion of stock outstanding	Number of companies							
	All officers				Total management (all officers plus nonofficer directors)			
	Railroads	Public utilities	Industrials	Total	Railroads	Public utilities	Industrials	Total
0 to 1 percent	31	27	38	96	23	16	22	61
1 to 2 percent	1	2	11	14	3	7	9	19
2 to 3 percent	2		9	11	3	3	5	11
3 to 4 percent		3	6	9	2	3	11	16
4 to 5 percent			1	1			5	5
5 to 10 percent		1	14	15	1	2	13	16
10 to 15 percent	1		2	3	2	1	8	11
15 to 20 percent			1	1			3	3
20 to 25 percent			1	1		1	5	6
25 to 30 percent			1	1			2	2
30 to 35 percent	1			1	1			1
35 to 40 percent							1	1
40 to 45 percent					1			1
45 to 50 percent								
50 and over		2		2		2		2
Total number of companies	36	35	84	155	36	35	84	155
Median	.04	.17	1.38	.40	.58	1.18	3.60	1.74
Arithmetic mean	1.47	3.91	3.05	2.88	3.64	5.35	6.40	5.52

[1] Source: Robert A. Gordon, "Ownership by Management and Control Groups in the Large Corporations," Quarterly Journal of Economics, LII (May 1938), p. 371. Stockholdings are based on Securities and Exchange Commission data and weighted in proportion to voting power.

For a large section of our economy it seems clear that the following generalizations hold: Industrial activity is typically carried on by large corporations and among these corporations ownership is widely dispersed.

TABLE VII.—*Average percentage stockholdings of management, by asset groups* [1]

Assets (unit: $1,000,000)	Number of companies			Percentage stockholdings of total management (unit: 1 percent)[2]		
	Railroads	Public utilities	Industrials	Railroads	Public utilities	Industrials
50 to 100	2	2	17	6.89 (6.89)	0.85 (0.85)	3.27 (6.19)
100 to 250	11	9	45	.82 (7.28)	1.03 (2.19)	4.57 (8.36)
250 to 500	9	10	13	.52 (2.23)	3.16 (10.20)	2.00 (2.51)
500 to 1,000	8	10	6	.48 (1.03)	.92 (5.86)	1.54 (2.63)
1,000 to 2,000	6	3	3	.88 (1.48)	1.74 (1.74)	2.71 (2.71)
2,000 and over		1			.07 (0.07)	

[1] Robert A. Gordon, Ownership by Management and Control Groups in the Large Corporation, Quarterly Journal of Economics, LII (May 1938), p. 37[illegible]. Total assets are net of depreciation and other offset reserves, as given in consolidated balance sheets for Dec. 31, 1935 (or nearest available date) and reported in Moody's Investment Manuals.

[2] Percentage figures not in parentheses are median holdings for companies in each asset group. Figures in parentheses represent arithmetic mean holdings. Medians are averages of the central 3 or 4 items in each group (depending upon whether the number of items in each group was odd or even). If there were only 2 or 3 items in a group, all were averaged to secure both mean and median.

[9] It should be noted, however, that even a small percentage of a billion-dollar corporation is a rather sizable sum when related to, say, the average per capita wealth of the nation.

Results of the processes of concentration of industry and diffusion of ownership.—Despite the recentness of its presentation, the theory of so-called monopolistic or imperfect competition has been rather thoroughly examined.[10] The generally accepted conclusions may, however, be repeated:

(1) All businessmen act like monopolists, limited by the extent of the control which they have over a particular market. The usual assumption is made that economic persons act in a rational manner and that rationality coincides with seeking to maximize profits.

(2) Most businessmen have an appreciable effect upon a particular market and hence have some control over it, though wide variations exist.

(3) The extent of the individual businessman's control over a particular market depends inversely upon the extent and effectiveness of competition.

(4) A monopolist tends to restrict production and raise prices above the level that would obtain if there were competition and the same level of efficiency on the part of the individual businessmen concerned.

To these should be added another point. Because of the lack of competition, a monopolist tends to respond relatively slowly to changed market conditions. This may be an admission of a lack of complete rationality in human nature, but it is based upon empirical observation. The monopolistic-competition theorists point out that monopolistic tendencies and evidences are graduated rather than suddenly becoming evident at the point when monopoly is reached. Thus we may expect a positive and continuous correlation between concentration of business, control over the market, and infrequency in price changes.[11]

Since the institution of the market exercises its control functions primarily through price, this will serve as a focal point for a brief examination of the extent to which administration has supplanted the market in its control over economic activity. A businessman and an economist maintain that "if common observation and statistics of industrial concentration may be trusted, some degree of jurisdiction over price by producers is all but universal." [12]

Gardiner Means distinguishes three factors underlying the extent to which administrative controls have supplanted those of the market:

> (1) At each stage the potential market for the particular product tends to narrow down * * *. As goods move from raw materials to finished products, the geographical market on the whole tends to narrow down. In a similar fashion the market for a particular raw material narrows down as it becomes more and more fabricated because of the narrowing of alternative functions for which it can be used * * *. Because of this narrowing down of the market at successive stages both geographically and functionally, it is usually possible for fewer and fewer producers to supply any particular market. It takes a million wheat farmers to supply the wheat market, a few thousand flour mills to supply the flour market, and only a handful of bakers to supply some rural town or small city with bread * * *. And as the number of separate enterprises supplying a particular market is smaller the administrative control over prices which can be exercised by each producer tends to increase * * *

[10] See, for example, Edward G. Chamberlain, Theory of Monopolistic Competition (Cambridge, Mass.: Harvard University Press, 1933), and Joan Robinson, Economics of Imperfect Competition (London: Macmillan, 1933).

[11] This follows naturally from the separation of price determination from the market. When removed from the constant higgling of a competitive market, we may expect prices to change less frequently. This does not necessarily mean, however, that the total price change over a period of time will be less if administratively controlled. Frequent price changes, such as those for wheat, may take place within a relatively small range.

[12] H. S. Dennison and J. K. Galbraith, Modern Competition and Business Policy (New York: Oxford University Press, 1938), p. 33.

(2) A second factor * * * is the large size of the efficient enterprise in many lines of activity * * *. Administrative control over price * * * tends to increase wherever efficiency in production requires large enterprises which reduce the number of independent producers required to supply the particular market. On the whole, this reduction in the number of separate producers appears to be a dominant factor in railroading and communication, highly significant in manufacturing, of minor significance in agriculture, and of varying significance in forestry and mining * * *.
(3) A third major factor * * * is collusion between separate enterprises or the bringing of whole industries under the dominant control of a single individual or group for the very purpose of exercising control over price.[13]

In relation to this last factor Dennison and Galbraith comment that—

several firms, each doing the same thing, can jointly reap additional returns over the pure competitive level of prices and production. As has sometimes happened in the past, they may be stimulated to get together to effect a control, but more often there is a tacit acceptance of the situation and a tacit and frequently unrecognized concurrence in a policy that effects the desired goal.[14]

Price leadership need not arise collusively; it can result merely from the knowledge that if one breaks below the existing price level others will follow and none of the concerns involved will profit. Thus there grows up the business feeling against the price "chiseler" even though the chiseler may be the only protection from excessive prices which the consumer has.

A brief examination of some price analyses will amply demonstrate that a great deal of the control over prices has passed from the market to the administrators. Under competition and a free market price, behavior should follow at least two general patterns. In the constant bargaining of the market, changes in demand may be expected to result in frequent changes in price in order continuously to move the supply. In the second place, a rather large drop in demand usually will result in a large drop in price, at least until a new equilibrium is reached in which the number of suppliers has been greatly decreased. Conversely, a rise in demand under competitive conditions will result in a rise in price, again at least until a new equilibrium is attained. The variation among prices in their sensitivity to changes in demand, as shown by the frequency of price changes and the extent of price change in relation to large changes in demand, will serve as an indication of the extent and location of administrative control over prices.

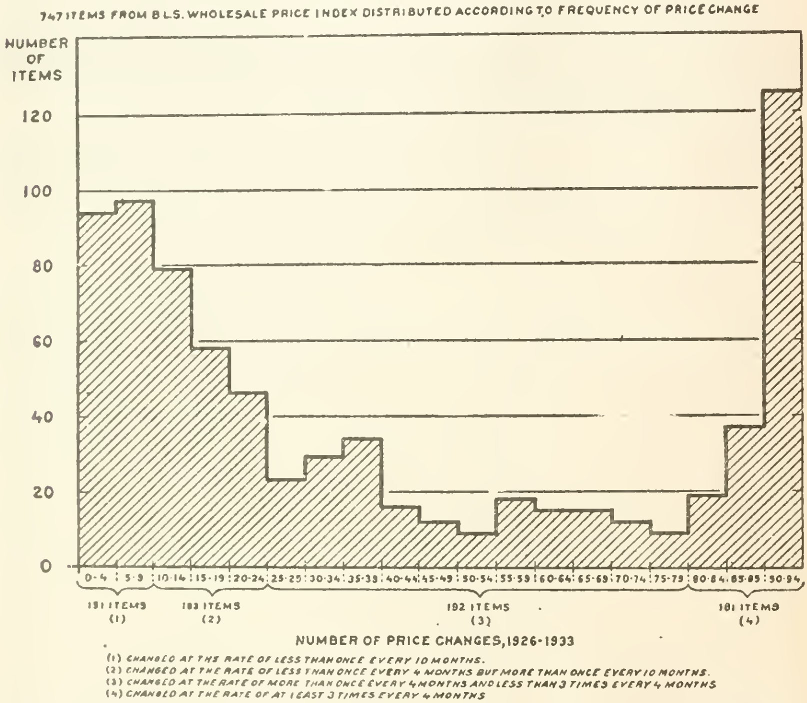
In a pioneering pamphlet[15] Gardiner Means related price inflexibility to the depression. In an analysis of the frequency of price changes during the period 1926–33, based on data of the Bureau of Labor Statistics, he found two principal types of industrial prices. One group changed frequently with changes in the market, sometimes every month, which is as often as changes are reflected in the Bureau's data. The other group changed infrequently, if at all, over an 8-year period. Commodities whose price changes lie between these two frequency groups were relatively few, considering the range of frequency involved. A graphic presentation of this price behavior is given in chart IV. Since "a producing unit acting alone can operate on a basis of administered prices only where it supplies a significant proportion of all the particular market or can narrow down the scope of the market by emphasis on special brands, trade names, and similar

[13] National Resources Committee, op. cit., pp. 144–45.
[14] H. S. Dennison and J. K. Galbraith, op. cit., pp. 34–35.
[15] Gardiner C. Means, Industrial Prices and Their Relative Inflexibility, U. S. Congress, S. Doc. No. 13, 74th Cong., 1st sess. (1935).

devices for differentiating the product of one producer from that of another in the minds of buyers,"[16] it is apparent that concentration has taken place with respect to pricing.

There is, moreover, quite a distinct relationship between the degree of administrative control and the magnitude of the total price change over a period of time. The variation in the magnitude of drop and rise in prices for different prices grouped according to frequency of change[17] during 1926–33 is shown in chart V. This chart covers the period 1926–38 and hence shows the price decline of 1929–33, the rise of 1933–37, and the drop of 1937–38. Group A had a price change

CHART IV—RIGID AND FLEXIBLE PRICES*



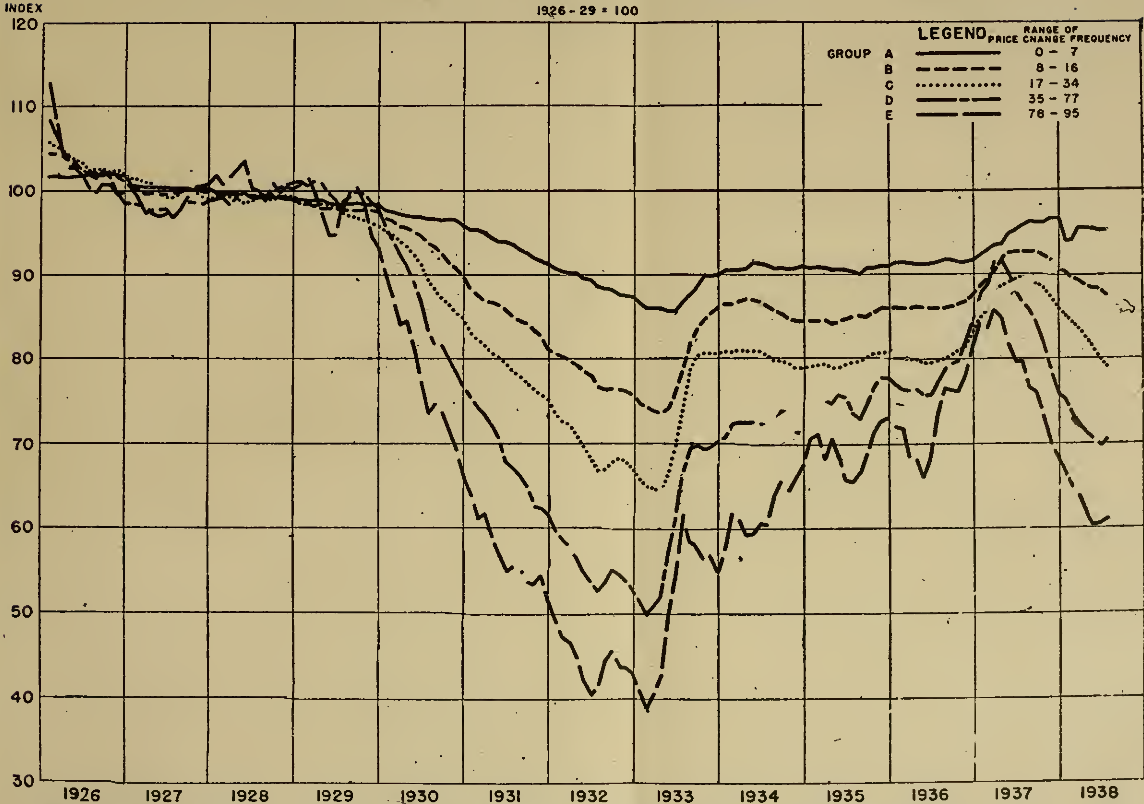
*From Gardiner C. Means, Industrial Prices and their Relative Inflexibility, U. S. Congress, S. Doc. No. 13, p. 2, 74th Cong., 1st sess. (1935).

frequency of less than once a year while group E includes commodities whose prices changed almost every month. The other groups lie between these two. Group A may be characterized as administratively controlled because of the infrequent changes and group E as market controlled. The chart clearly shows that administratively controlled prices were held fairly constant during the period, while market controlled prices, on the other hand, responded with wide changes in price to changes in demand.

But price is only one of the possible means of adjusting to changes in demand. Such adjustment can also be made through changes in production. One might suppose that in the case of administratively maintained prices a fluctuation in production took place. Chart VI shows that this is the case. For the administered-price group there

[16] National Resources Committee, op. cit., p. 110.
[17] Frequency of price change serves as a good index of administrative control.

CHART V.—MONTHLY WHOLESALE PRICES FOR 5 FREQUENCY GROUPS 1926–38 [1]



[1] From National Resources Committee, The Structure of the American Economy, Part I (Washington: Government Printing Office, 1939), p. 147.

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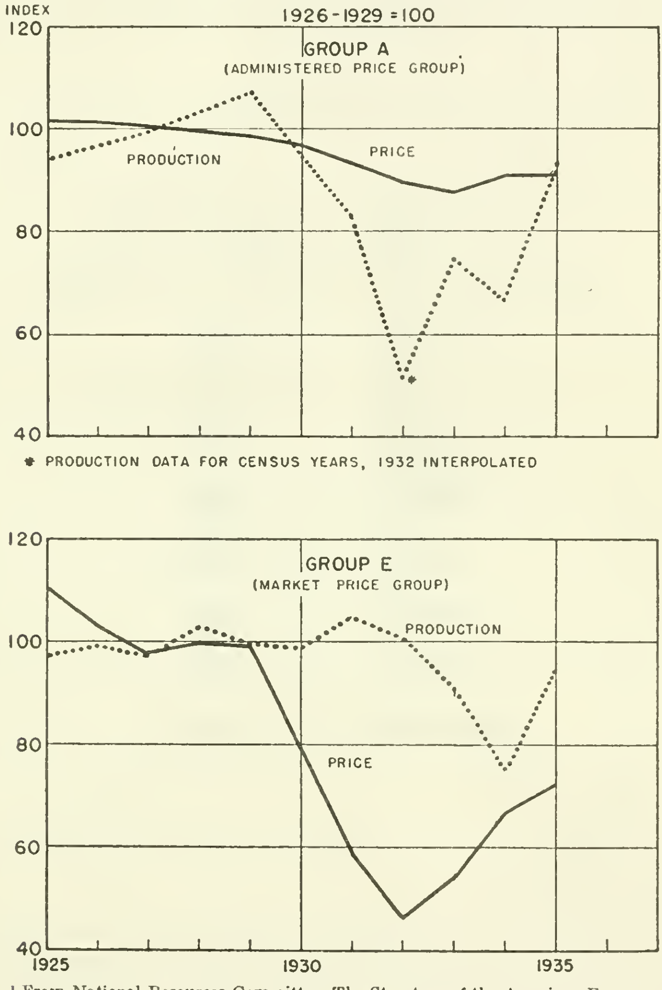
[16] National Resources Committee, op. cit., p. 110.
[17] Frequency of price change serves as a good index of administrative control.

was a decline and recovery of production during 1929–35; for the market-price group the decline and recovery was primarily in terms of price. Chart VII shows price and production behavior for 10 major industries during the period 1929–37. Here it is demonstrated

CHART VI.—PRODUCTION AND PRICES OF ADMINISTERED AND MARKET PRICE COMMODITIES [1]



[1] From National Resources Committee, The Structure of the American Economy, Part I (Washington: Government Printing Office, 1939), p. 148.

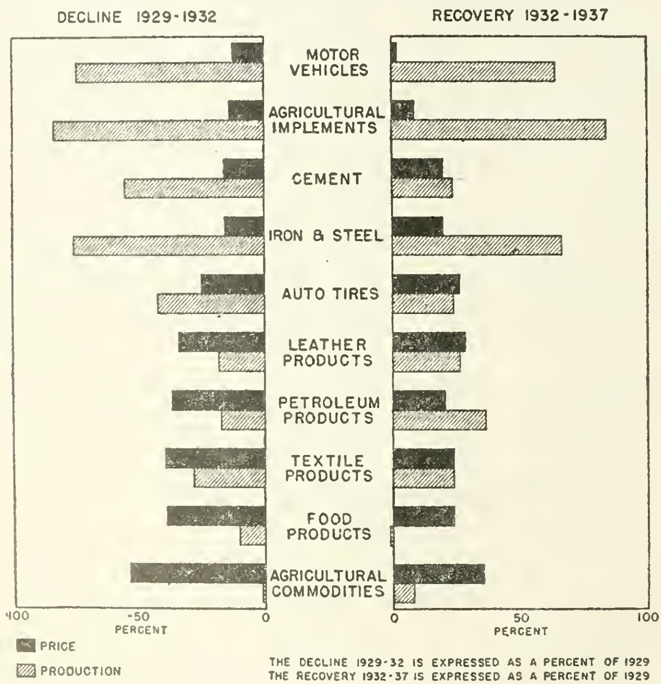
that the adjustment to depression took place largely through variations in production of motor vehicles, agricultural implements, cement, and iron and steel, while food products and agricultural commodities were adjusted largely through price.

This brief perusal of price behavior [18] should be adequate to demonstrate that administrative control over prices permeates a rather large portion of our economy with substantial effects on levels of prices

[18] For an excellent, detailed examination of this subject, see National Resources Committee, op. cit., pp. 122–152, 173–269.

and production. Two related conclusions which are of significance for our present study may then be stated. First, it is apparent that for a large section of our economy, market controls no longer operate. Thus this protection of the public against excessive prices and production below the social optimum has to a considerable extent disappeared.[19] Secondly, in those areas where administrators control prices there must be an effective sense of responsibility to the public, a sense of business trusteeship to insure that the administrative control of prices, production, and hence also employment, does not

CHART VII.—PRICE AND PRODUCTION CHANGES DURING DEPRESSION AND RECOVERY FOR 10 MAJOR INDUSTRIES[1]



[1] From National Resources Committee, The Structure of the American Economy, Part I (Washington Government Printing Office, 1939), p. 141.

result in a level of production substantially below what is readily attainable and that undue rigidity does not accentuate and prolong depressions. If this sense of responsibility to the public and its welfare is absent or ineffective, then means must be found whereby its effectiveness may be attained. Otherwise America will malinger under a standard of living lower than that which it could and should have. In other words, we need a maximum of the benefits of concentration and large-scale production with a minimum of its ills.

[19] Dennison and Galbraith maintain that "when the individual producer can influence price, the self-regulating character of competition, by this very process itself, is impaired or eliminated. When price is beyond the control of the producer, as in agriculture generally, it is an objective specification indicating the amount which society regards as the optimum to be produced * * *. But if the producer has the power to alter price, then the specification is no longer set by society, but by himself. Quite naturally he forms his price policy with his own interest in mind; it is an accident if the social and the individual interest coincide * * *. Wherever there is individual jurisdiction over prices there is the same incentive as there is under monopoly to produce less than the socially desirable minimum."—H. S. Dennison and J. K. Galbraith. op. cit., pp. 33–34.

CHAPTER III

THE SEPARATION OF OWNERSHIP AND CONTROL

Another result of industrial concentration and the diffusion of ownership is so important that it deserves special consideration. It is the separation of ownership from control. Theoretically, of course, the holders of a majority of the voting stock control a corporation. But "the assumption that the owners of common or voting stock control a company is for the most part a fiction so far as the large corporations listed on exchanges are concerned."[1]

Three general types or sources of control may be differentiated: control by the holders of a majority of the voting stock, control by an active minority, and control by management. Control by means of a legal device, such as a holding company, may usually be resolved into one or the other of the last two types, especially when one considers the proportionate interest of the dominant group in the securities of the bottom company.[2]

We have already seen how rarely an individual or a small group owns a majority of the stock of one of the giant corporations.[3] Unless there is a powerful nucleus of some sort, it is practically impossible for the hundreds or thousands of scattered holders of a majority of the stock of a giant corporation to get together, even by proxy, in order to exercise a degree of control. Moreover—

> The individual stockholder does not know the merits of those who contend for the control of the directorate; he has little or none of the materials which might enable him to judge by results. Earnings may be good or bad because of the competence or incompetence of the officers; but they may be good or bad, also, because of the good or bad condition of business in general.[4]

Thus the small stockholder is not in a position to act decisively or even to know how to act were he in such a position. So long as he receives satisfactory dividends or at least convincing reasons why such returns are not forthcoming, the average stockholder will return his proxy certificate to the existing management or the group in control, if he sends it to anyone. The control of the scattered majority, in those rare cases where it is effective, is cataclysmic rather than continuous. The existing dominant group in the typical large corporation must sin greatly before the judgment of the majority breaks around its head. Thus, within extremely broad limits, which in practice are rarely reached, control by a group other than the majority stockholders is the typical situation among the corporate giants.

[1] John C. Baker, Executive Salaries and Bonus Plans (New York: McGraw-Hill, 1938), p. 2.
[2] The extent to which ownership by the control group in the bottom companies of a holding-company pyramid may be carried is illustrated by the former Insull colossus. At one time, Insull interests controlled some of the bottom companies with as little as two-hundredths of 1 percent ownership of the securities of these companies. Yet at only one step of the many-tiered pyramid did Insull have less than a majority of the voting stock of the holding or operating company next below. See Federal Trade Commission Utility Corporations, No. 72-A (1935), p. 160.
[3] Supra, pp. 10 ff.
[4] H. S. Dennison and J. K. Galbraith, op. cit., p. 68.

Minority control is much more common than majority control among the large companies. It arises where a compact group owns a substantial but minority interest which constitutes a majority of the stock actually represented at stockholders' meetings, or to which the control group can attract a sufficient number of proxies from scattered holders to constitute a majority at such meetings. The latter rather than the former is the usual means of minority control.

Once in power a minority group is difficult to dislodge. It has, of course, picked a management which is congenial and cooperative. Then the proxy machinery, with expenses paid by the company, is commonly at its disposal. The proxy committee is in effect chosen by the control group and is used as a means of perpetuating itself. Naturally, the larger the corporation and the more dispersed the stock, the more difficult it is for a noncontrol faction to amass a sufficient number of proxy certificates to oust the control group and assume command.

As long as management is cooperative with the minority control group, therefore, the minority is relatively secure in its power. When however, the minority and the management disagree, a major battle may impend in which the management holds a powerful and strategic position. In the ensuing struggle for proxies the management may deny the use of the proxy machinery to the minority, which is then faced with formidable obstacles. The expense of circularizing stockholders with arguments sufficiently convincing to result in their sending in proxy certificates to the minority is a considerable item when stockholders are numbered in thousands. Then there is the natural tendency of the stockholders to let well enough alone and to vote for the existing management, if they vote at all. Thirdly, there are always two sides to the arguments, and to many the side of management may be the more convincing.

The implications of a closely fought battle between a minority control and the management have never been more dramatically demonstrated than in the successful attempt of John D. Rockefeller, Jr., to oust the management of the Standard Oil Co. of Indiana in 1929. Colonel Stewart, the head of the management, was implicated in the oil scandals of the Harding administration and Rockefeller asked him to resign. He refused, and the rest of the board stood by him. The result was a battle for proxies for the next election of directors, with Rockefeller denied the use of the proxy machinery. With his prestige, arguments, and a nucleus of about 15 percent of the outstanding stock which was held by his interests, Rockefeller was able to oust Colonel Stewart.[5] The effort is reported to have cost Rockefeller $300,000.[6]

The situation when the management acts successfully against the wishes of a large minority stockholder is illustrated in the struggle between J. P. Getty and the management of Tide Water Associated Oil Co. Getty sought to make the directors more responsive to the stockholders.. However, in spite of his apparent control of about 35 percent of the stock of Tide Water, Getty lost not only the resulting proxy battle by a wide margin, but was unable to get the directors of the Mission Corporation, which he presumably controlled, to vote the corporation's holdings of Tide Water in his favor. In regard to the latter, Getty and his associates held 44½ percent of the stock of

[5] See New York Times, various issues from January 12 to March 8, 1929; and A. A. Berle and G. C. Means, op. cit., pp. 82–84.

[6] One oil executive has remarked, "With $300,000, I could buy the proxies of any large corporation in the country."

Mission,[7] which constituted the only significant stockholder interest.[8] Yet the directors of Mission voted the corporation's 20 percent holdings of Tide Water in opposition to Getty. Thus not only did Getty fail to win his battle with the Tide Water management, but the directors of Mission dared to act against his will. It should be noted, however, that the personnel of the board of Mission was subsequently largely replaced.

Additional instances of minority-management controversy could be cited, but these serve to illustrate the precariousness of the minority's control when management is antagonistic. In the great majority of the cases, however, management and the minority work harmoniously together, sometimes making concessions [9] but on the whole acting as a team.

The most common form of control among the large corporations may be termed management control. When stockholding is sufficiently diffuse the position of management becomes almost impregnable.

Management does not need to own stock; the strategic advantages of its location are quite sufficient. A presumption of worth is in its favor and, more concretely, the proxy machinery is at its disposal. Management chooses the proxy committee and by making appointments from among the members of management assures its own continuance. The effectiveness of this machinery is too formidable for small stockholders to overcome. The Financial Editor of the Chicago Daily News, for example, describes the situation thus:

> Taking industry as a whole, the methods of using proxies gives the average stockholder about as much chance to express an opinion as a Chinaman would have of choosing the President of the United States. He can agree or keep still. The proxy which is sent out lets him vote for the management: if he objects he can come to the meeting and register a kick. When he gets there he will be in the minority.
>
> The management usually enters the meeting with enough votes to carry any measure, regardless of those present.[10]

Only the cataclysmic uprising of an indignant majority of the stockholders is sufficient to overthrow the management. And before such a crucial stage is reached even a not too astute management will usually have made concessions, sometimes of a quite minor nature, which are adequate to prevent the revolt. In business as in politics, taking the enemy into camp often works admirably in extending peace between groups.

TABLE VIII.—*The location of control of 200 large corporations* [1]

	By number	By wealth
	Percent	*Percent*
Management control	44	58
Legal device	21	22
Minority control	23	14
Majority ownership	5	2
Private ownership	6	4
In hands of receiver	1	(2)
Total	100	100

[1] From Adolph A. Berle, Jr. and Gardiner C. Means, The Modern Corporation and Private Property (New York: Macmillan, 1932), p. 94.
[2] Negligible.

[7] New York Times, May 8, 1936.
[8] Securities and Exchange Commission, Official Summary of Holdings of Officers, Directors, and Principal Stockholders, p. 115.
[9] See, for example, the rapprochement between the management of Armour & Co. and Mr. F. H. Prince after he had demonstrated his obstructional power and increased his stockholdings; New York Times, December 14 and 17, 1933.
[10] Royal Munger in the Chicago Daily News, January 20 and March 7, 1939.

In their study of 200 large corporations, Berle and Means summarized their findings as to the location of ultimate control of the giants as shown in table VIII. Since control through a legal device is usually either minority or management control if traced back far enough, control by groups owning less than a majority of the stock dominated about 88 percent of the companies representing about 94 percent of their wealth, and of this portion management control is paramount.

The relatively helpless position of the dispersed stockholders makes it imperative that those in command of the large corporations consider the rights of these disfranchised citizens of the economic community.[11] In other words, the dispersion of stock ownership requires, in the interests of justice, that the control group act not only in its own interests, but also as a trustee for the interests of those who are unable to make their demands effective. A 1928 statement by a subsequent chairman of Marshall Field and Company and chairman of the board of the American Management Association may be appropriately repeated. James O. McKinsey commented that the dispersion of stock ownership—

> has brought about the situation in which the board of directors acts in a fiduciary capacity. If they fully realize their responsibility, this naturally leads them to exercise closer supervision over the activities of the business than if they were not representing a large group who were not familiar with the activities of the business and who were not exercising any responsibility for the management of the business other than selecting the directors to represent them.[12]

It must be recognized, on the other hand, that it is not easy for the control group to give consideration to the interests of the scattered stockholders. One important reason for this is that their interests may be divergent. The concern of management with high salaries may result in lower dividends to the stockholders than would otherwise be possible. Or again, since those in control of a corporation are the first to gain information which will have an effect upon the value of the stock, the insiders may be able to buy or sell in such a way as to make substantial profits at the expense of those who are induced to sell or of new stockholders who are induced to buy without having inside information. While section 16 (b) of the Securities and Exchange Act of 1934 is a real obstacle to many such transactions, it does not affect a group of nonofficer stockholders who individually own less than 10 percent of any equity issue, but who together own a more substantial interest. Those in command may also be in a position to direct purchases, sales, and other transactions into channels which will be profitable to individual members of their group. This is particularly true if a holding company with several subsidiaries is used as the control device. Such practical limitations must be kept in mind when speaking of making trusteeship effective.

The ascendancy of management.—With the diffusion of ownership which we have noticed in a large sector of our economy, management is left with the responsibility for determining policies, including those affecting prices, production, and employment, within very broad limits and for all practical purposes without effective check from any source. When there is a degree of concentration of stockholdings, of course, the important stockholders may take part in determining

[11] To be sure, trusteeship is inherent, and does not arise from the great number of small stockholders, but it is emphasized by their helplessness.
[12] James O. McKinsey, Functions of Boards of Directors, Board Committees and Officers, General Management Series: No. 82 (New York: American Management Association, 1929), p. 3.

broad policy, either through direct informal contact with the management (including the directors) or through choosing directors who will adopt the desired lines of action. Even here, however, the directors need not be responsive to the demands of those who elected them. Except in those relatively rare cases where the charter provides for removal, the directors are practically unfettered in making their decisions until reelection time comes. And in the large proportion of the corporate giants where management rules supreme, even election time is no cause for particular concern, for the means of returning themselves to office are securely in their own hands.

What sort of economic empires have been thereby set up? Are they monarchies or oligarchies? To what extent is policy formation brought to a focus? The rather intensive investigation of a limited number of giant corporations and the more cursory view of a larger number made by the authors will permit few generalizations answering these questions, although tendencies may be noted. Two generalizations, however, may be presented. These are (1) large boards rarely function effectively as units; yet, on the other hand, (2) giant corporations actually run by one man are fully as rare. In economic as in political empires the contributions of several minds are essential to success.

A common role which the boards of directors of the large corporations play is that of serving as ratifying bodies for the decisions of the executives. The board members either do not have the time or the interest to take a very active part in the formation of managerial policy. One student of industrial administration, for example, has said:

I have always found that the only thing boards of directors are interested in getting from an operative or production manager is statistics of savings, increased profits, lower operating expenses. They are not interested in how it was done or how the worker or others felt about it. They are not interested in plans you may have or how the executives are going to continue the process because the process has to be continued if the executives' reports are going to be satisfactory.[13]

Our study of the management of giant corporations has indicated that Diemer may have somewhat overdrawn the picture, but that for boards functioning as a unit there is a clear tendency in the direction which he indicates. There are, of course, wide variations. Two executives of two giant corporations illustrated the extremes of board activity in interviews. One said:

Board meetings are rare and they never do anything important. We hardly know that the board exists, and I doubt whether a half dozen employees could tell you who the members are.

On the other extreme, the second described the activities of the board of his company thus:

Until a short time ago the board met regularly five times a week. It still dispatches much detailed business. For example, five possible packages for——— are put before one of the board members. He picks the one he favors, the board concurs, and he orders the president of the proper subsidiary company to go ahead with production.

Comments such as "The board serves as a reserved control"; "The board can't control; no one except management knows enough about the business to ask intelligent questions"; "There are few cases in which the board has been asked to determine direction," were common

[13] Comments of Hugo Diemer, of the La Salle Extension University, in James O. McKinsey, op. cit., p. 16.

The typical board as a unit in the large corporation appears to exercise little authority of a continuing nature. In roughly three-fourths of the companies examined on this point the board had only a small role to play.

In the other corporations where the boards were more active there was commonly a heavy sprinkling of members who were officers. In these cases the increased activity on the part of the board seemed to arise chiefly out of the officer members getting approval for action taken or to be taken in their respective departments—matters which in other companies were decided without reference to the board.

The functions of the boards may be related to their composition. Of the 20 largest industrials, the 8 largest utilities and the 8 largest railroads of Gardiner Means' list of large corporations,[14] approximately half have boards with more than 15 members. There is little variation in this median among the groups. The boards range from 4 members for Ford to 36 for E. I. du Pont de Nemours. It has long been found difficult for such large boards to function as units.[15]

An examination of the boards of these companies also shows that there is wide variation in officer [16] participation. Some of the companies had only one officer on the board while in others, the board was composed entirely of officers and those closely associated with the executives.[17] The variation for this small group of companies is shown in table IX. This indicates that railroads most frequently have nonofficer boards, utilities follow with nonofficer and mixed boards, while there is not a clear emphasis on either officer or nonofficer boards among the industrials.[18]

TABLE IX.—*Officer participation on boards of 36 giant corporations*

General classification of boards [1]	Number of companies			
	Industrials	Utilities	Railroads	All
Officer board	8	1		9
Mixed board	5	3		8
Nonofficer board	7	4	8	19
Total	20	8	8	36

[1] Basis of classification: Boards were classified as "officer boards" when they were composed of 60 percent or more officers, as "mixed" when the percentage of officers was from 30 to 60, and as "nonofficer" when the percentage was below 30. The slightly larger span of percentages for the officer boards was deemed conservative because in many cases board members were either past officers or officers of subsidiaries and hence were closely related to the given officers even though not classified as such. Moreover, officers may be expected to be more active on boards and to attend meetings more regularly.

In the case of the railroads, management has become quite professionalized, and increasingly remote from ownership, which is widely diffused. Yet the companies need many outside contacts, including financial ones, and the boards serve this purpose. A somewhat similar position is that of the utilities. The industrials, on the other hand, have not felt the same need for public contacts, nor are they subject

[14] The list is given in National Resources Committee, op. cit., pp. 100–101.

[15] E. A. G. Robinson expresses it a little too patly but there is some truth in his statement: "Anyone who has ever done business with committees knows that 5 people can reach a decision, 15 people can be persuaded by a man who has made up his mind, and 25 people are a debating society."—The structure of Competitive Industry (New York: Harcourt, Brace, 1932, p. 48).

[16] An officer is here defined as one of those listed as such in Moody's Annuals.

[17] For example, the presidents of subsidiaries are frequently on the boards of the parent companies even though they are not strictly classifiable as officers of the top company.

[18] Several prominent industrialists expressed their opinion in interviews to the effect that the trend was clearly in the direction of replacing nonofficers with officers on the boards.

to so complete a separation of ownership and management, for some of the large industrials are still closely held.

In those cases where there is a large proportion of officers on the board, such members naturally find it difficult to separate the functions of their two positions. Consequently, administrative detail may be brought up for board action and decisions may be made on the basis of administrative convenience rather than upon considerations of general policy viewed with broad perspective. The board typically acts on the recommendation of the interested executive.

The boards of the giant corporations, then, provide a final and often perfunctory review of administrative action, past or contemplated, and have a varying influence in the choice of executives. In a formal way they pass on a multitude of items but most of this business is approval of committee or executive recommendations handled in a routine manner or after a merely cursory examination. There are, of course, variations, but on the whole this appears to be the typical picture.

Board committees, on the other hand, are often more active and of more positive influence than the boards as a whole. Their power, of course, stems from the tendency of boards to approve the recommendations of their committees, but this does not destroy their influence. Approval is typically almost routine in nature. As a consequence a small group on a strategic committee may wield a great deal of influence, particularly in the field of its specialty. A small finance committee, for example, was considered the main power in Armour & Co. of Illinois for a decade.[19] There are two influential committees in the board of Du Pont: The finance committee has supervision of the extensive investments of the company and the executive committee concerns itself with the operative side.[20]

Other corporations show particular committees in places of special influence. They may be called the finance committee, the executive committee, the policy committee, or by some other name. Regardless of the designation, however, they serve as bodies whose recommendations are commonly adopted by the board.

Sometimes a committee is set up composed chiefly of officers.[21] This group may advise on almost all broad policies or, on the other hand, may be limited to suggestions on handling administrative problems and to pointing out the managerial implications of contemplated action. A board composed of officers may be considered a sort of superexecutive committee, acting on its own recommendations and responsible in varying degrees to itself and to the chief executive officer of the company. Thus, a sort of circular relationship exists wherein "the board appoints the officers and the officers appoint the board." [22]

Control is not necessarily fixed at one point or vested in one person. It shifts from one point to another depending upon the subject matter involved in the particular decision. This may be illustrated by General Motors. The chairman, Alfred P. Sloan, is especially concerned with engineering and sales; the vice chairman, Donaldson Brown, controls financial operations; and the president, William S. Knudsen, who is also chairman of the administration committee, is

[19] New York Times, December 16, 1933.
[20] Fortune, X (December 1934), pp. 88–89.
[21] This is illustrated by the administration committee of General Motors and by the advisory committee of nonboard officers of General Electric.
[22] Stated in an interview by an executive of a company with an officer board.

primarily concerned with production. Outside groups such as financial institutions and labor unions may also exercise control over policy in their respective fields.

Even where a company appears to be a one-man show, further examination reveals that the one man is dependent for his decisions upon the recommendations of his subordinates. The modern corporation has become too large for one person to know all the details of its activities and of the varying social conditions in which it must operate. Consequently, the senior officers serve as a sort of advisory staff to the chief executive official. Because the chief executive official cannot go into the detailed implications of all decisions, he must depend upon his subordinates to give him the right information and to suggest decisions. In fact, many chief executives maintain that picking the right men is the most important part of their job. Thus, one-man decisions are almost always group decisions when one probes beneath the surface.

Despite the limitations on concentration of policy formation and the various more diffused forms that it may take which we have pointed out, the chief executive official remains, in the typical case, the most influential individual in the determination of policies. It is sometimes said that he sets the tone of the whole enterprise. He is not, however, always easily identified. He may be the president or he may be the chairman.[23] It depends upon the tradition of the company and the personal influence of the incumbents of these positions. There is usually a two-fold division of the top managerial duties. If the chief officer is the president, there will often be a senior vice president who concentrates on problems of operation. If he is the chairman, the president will usually be an operating man.

Policy formulation and policy execution may be distinct concepts, but it is not possible to separate them according to the position of those who perform these functions. Pointing out tendencies and emphases is as far as one may go. At one time the president, for example, may give orders which place him in the stream of policy execution. At another time he may make decisions or recommendations which can be classified only as part of the process of policy determination. In general, the chief executive official of the large corporation is more concerned with policy than is his senior subordinate. It must be remembered, however, that both take part in the process and both must draw upon the advice of others in reaching their decisions. The chairman or president, with the board, may set the final stamp of approval upon the production quota, for example, but this action is based upon the recommendation of the production vice president or similar officer, who in turn has drawn for his material upon the contributions of his subordinates.

What then is a summary statement of the extent to which policy determination is brought to a focus? Perhaps on the basis of our study only this can be said. The diffusion of ownership has given management a predominant voice in policy formulation as well as in policy execution. The determination of policy has its base in the contributions of many individuals, but the process comes to an approximate focus in a few. Even though one man may be the most influential member of the group, and may in some respects be said really to run the enterprise, the contributions of others retain some of their

[23] Frequently, of course, the two offices are combined.

identity. The finance committee may recommend prices and the production manager or operative officer suggest quotas. The result reached from a consideration of these factors is the determinate of the volume of employment so far as internal decisions are concerned. Corporate policies are thus characteristically group policies, though they may bear the clear imprint of only small groups and of influential individuals.

The implications for bureaucracy and trusteeship may be stated in broad terms. The dominance of management results in a decline of outside checks. This in turn may contribute to the growth of the undesirable aspects of bureaucracy. The effect of many individuals in the determination of policy means that the sense of trusteeship must penetrate below the top level. The focus of the process of policy determination carries the necessary implications that too much emphasis should not be placed upon holding some one man responsible, and that whatever devices for enhancing the effectiveness of trusteeship may be suggested, they must be such as will affect at least several individuals in each concern, the identity of whom varies from corporation to corporation.

The obtrusion of bureaucracy.—A final result which may be expected of the growth of big business and the diffusion of ownership is the development of bureaucracy within large corporations. Human nature has certain characteristics which persist, almost regardless of environment. When the environments of both business and governmental employees present such common attributes as large size, impersonal relationships, standardized salary remuneration, a body of administrative rules and procedures, and the like, it is not surprising that they often react in corresponding ways. Corporation executives who have given thought to the matter are practically unanimous in admitting that bureaucratic tendencies (sometimes called organizational resistance) are operative in big corporations. In those cases where the executive believes that these tendencies have been largely neutralized, they maintain that it is due to positive counteractive measures which have been taken. We shall deal with these later. First, however, we must analyze and attempt to explain the cause of bureaucratic characteristics which executives agree do exist in big business.

PART II

CAUSES AND MANIFESTATIONS OF BUREAUCRACY

CHAPTER IV

THE CHARACTERISTICS OF BUREAUCRACY

The discussion of bureaucracy has commonly generated more heat than light. It is a term of opprobrium. In popular parlance, bureaucracy is bad, rarely good. On the other hand, the term has a technical, literal use which makes it indispensable in the description and analysis of large social aggregations. When employed in this sense, bureaucracy loses its good-bad connotations and is merely a verbal reference to a complex social situation possessing certain formal characteristics and institutional objectives. When thus reviewed, we may say that an aspect of bureaucracy is desirable or undesirable, but only from the standpoint of the objectives sought. In the discussion of the subject which follows, however, it will be difficult to dissociate the popular, opprobrious connotation from the technical, analytical use of the term because we must take account of popular attitudes as indicators of underlying difficulties. All we can do, therefore, is to attempt to differentiate the two uses as occasion requires.

Bureaucracy is characterized by successive departments, bureaus, and other subdivisions arranged in a hierarchy, each with its own particular sphere of activity and interest, and under the control of a chief. To these attributes—a subdivision of jurisdiction and a hierarchy—Carl J. Friedrich and Taylor Cole [1] add a third: professionalization of personnel.

It is apparent that bureaucracy, defined in these terms, is very widespread.[2]

Whenever a large number of persons are brought together for the purpose of accomplishing an objective, it is essential that some direction be given to their efforts and that individual objectives be either subordinated to or harmonized with those of the group. For these purposes a hierarchy is established.

A system of hierarchy is as characteristic of business as it is of government, and in some respects the corresponding powers of the superior officers are more absolute in business. It is true that for crimes such as high treason, the state may deprive a person of his life. But for the great bulk of disciplinary action within a governmental hierarchy, the sanctions are no stricter than those of business and their application is surrounded by limitations. The private administrator, on the other hand, may deprive a subordinate of his means of livelihood almost at will and with few, if any, procedural requirements. In fact, the system of hierarchy and relatively unfettered authority is widely defended as an essential part of successful business administration.

[1] Carl J. Friedrich and Taylor Cole, Responsible Bureaucracy (Cambridge, Mass.: Harvard University Press, 1932), p. 18.

[2] For an affirmative argument that there are general principles of administration applicable to all social groups, see the books of two General Motors executives, James D. Mooney and Alan C. Reiley, Onward Industry! and The Principles of Organization (New York: Harper, 1931 and 1939).

Similarly the distribution of functions and activities among departments and their subdivisions is an accepted administrative method in business as in government. In business the means whereby these activities are allocated varies somewhat. The scope of a particular department may be determined by superior authority or it may be left, within limits, to be decided by the department heads according to their individual capacities, interests, and aggressiveness. As an ideal, the first method, supported by staff study, is frequently held by corporation executives to be the more desirable. In actuality, however, the second method enjoys wide vogue, particularly at the top levels of the administrative hierarchy. In either case a means is provided whereby the scope of a department's jurisdiction is defined, even though its borders may be somewhat indistinct and transitory.

In the establishment of determinate qualifications for executive personnel, which Friedrich and Cole mention as a third characteristic of well-developed bureaucracies, there is a considerable diversity of practice. But among the large corporations there are distinct elements of such a tendency. Among the railroads, for example, executives are recruited almost entirely from within a given company or from other railroads. This practice is less strong but still present in the utilities, and is least prevalent among the industrials. Where ownership and management are separate—which is characteristic of the largest corporations—it is the boast of the executives that they are professional administrators. Nevertheless, there is a felt need for a better classification and record of executive requirements and capacities.[3] Though professionalization of management in private business varies, it is present and welcomed by those in control of the larger corporations.

To the extent, then, that these elements—distribution of functions, hierarchy, and professionalization—constitute the essential characteristics of bureaucracy, this term describes large-scale private business as accurately as it does public administration. There are, however, other characteristics of administration which are included in the concept of bureaucracy when used as an invidious term. These appear to stem from the more fundamental aspects which we have mentioned and are perversions, improper functionings, or undesirable accompaniments of them. The more important merit examination.

The most general criticism of bureaucracy is its unresponsiveness to the demands of the public and to hierarchical superiors. Thus, Friedrich and Cole have commented:

> We condemn as bureaucratic the delay and lack of response from the representative of a large organization, whether public or private, because we do not sympathize with or do not understand at all the ultimate objective or combination of objectives which this organization is supposed to realize. In such situations the word "bureaucracy" is widely used to decry acts of officials which, while required for the sake of "Efficiency," are cumbersome and irritating to the person subjected to them. * * *
>
> Since the government is by far the largest single organization of this variety, the cumulative effect of such experiences has in the mind of most people prevented any realization of the fact that a church, a trade union or a business corporation tends to show the same characteristics. * * *
>
> It is easier to overestimate than to underestimate the difference between such governmental bureaucracy and the church bureaucracy, the party bureaucracy, or the bureaucracy of the business corporation. Much depends upon the cir-

[3] See, for example, Edward R. Stettinius, Jr., "The Selection of Executives," Management Review, XXV (November 1936), pp. 332–33.

cumstances of time and place. * * * Any large body of men organized for common action will tend to act in a way which will appear arbitrary and therefore irrational to the outsider, although the particular act may be completely rational when looked at from within.[4]

The take-it-or-leave-it attitude on the part of the trusts contributed largely to the movement to control them. Just as the monopolies were not destroyed, however, neither was the attitude, though in many cases it was softened or became more suave. It took highway and air competition to wake the railroads to the importance of the passenger. That paragon of service, the filling-station employee, is directly related to the ease with which the motorist may drive to another station. The threat of public ownership has been a prominent reason for the emphasis upon public relations in the telephone industry. In those monopolistic or semimonopolistic areas where no such threat of competition exists, on the other hand, it is only natural to find a lower degree of responsiveness to public desires.

To the extent that unresponsiveness within the hierarchy exists, the purpose of the organizational structure itself is not being wholly fulfilled. The executives of the large corporations almost universally admit in interviews that they find varying degrees of organizational resistance among their subordinates, and that drastic means are sometimes necessary in order to overcome this tendency.

Unresponsiveness, it should be noted, is a broad term which includes four other more specific aspects of bureaucracy. These are an excess of rules or legalism, maladjustment of the working parts of the organization, a low level of morale, and the tendency of persons and organizational units to enhance their own importance.

The extensive use of more or less rigid and precise rules and working procedures is well-nigh universal among the giant corporations. In no other way can such large administrative units be made to operate consistently. However, what may be necessary from an administrative viewpoint is often irksome to the public, which does not understand the administrative implications of a given order. "Sorry, it's a company rule," doesn't help to make an exasperated customer feel that his particular case is being treated with much consideration. Within a corporation, furthermore, subordinate officials often complain that they are not permitted sufficient discretion, that transactions of any size must be referred through too elaborate channels. When questioned on this, however, the superior officials are quick to point out that there are aspects of such transactions which subordinates cannot understand. For consistency and safety, therefore, the top executives claim that limitations are necessary. Indeed, a whole philosophy of management—that of scientific management—is largely predicated on the idea of elaborate rules established for the most simple and routine actions. An unwieldy body of regulations is thus inevitably built up, and it becomes easy to forget the objectives of the system in a blind obedience to rules.

Maladjustment of the working parts of an organization is also frequently cited, both in business and in government, as evidence of the evils of bureaucracy. Instances are adduced where one part of a hierarchy worked at cross purposes with, or wasted its efforts by duplicating the efforts of, another. Illustrative is a case brought out in an interview. The company concerned is subdivided on the basis

[4] Friedrich and Cole, op. cit., pp. 1, 2, 14, 22.

of products, though there is great similarity among them. Nevertheless, the officials of one division frequently consult with outside competitors on research, production, and other problems rather than attempt to discover what colleagues in their own concern had done along those particular lines.

It is anomalous that this malcoordination should be called a characteristic of bureaucracy. It exists because an essential purpose of bureaucracy, the coordination of effort, is not being fulfilled. Such, however, is the common conception. No official either of a large corporation or of government would claim that complete coordination exists in his organization. This lack, therefore, is attributable to the failure of bureaucracy rather than to its active effect.

A low level of morale is also considered part of the typical picture of bureaucracy. The bureaucrat is viewed as weighed down with rules, procedures, and red tape, mired in his own particular rut, uninterested in getting out of it and unable to do so if he would. Likewise he is loath to exert any great effort to advance the work of the enterprise.

The level of morale at a given time is difficult to measure because it is comparative and its elements are largely subjective.[5] Many executives, however, will admit that the morale of their employees is not especially high or that it was very low before a particular personnel policy was adopted. Among the corporate giants the company with a high level of morale is indeed rare. On the basis of interviews and observation, there appears to be a medium level around which most of the employees cluster. Extra time and effort in cases of emergency are grudgingly given. Some officials complain that potential executive material is destroyed by the dulling environment at the lower levels of the hierarchy, causing irreparable loss to the company and employees concerned. Others say their men are in a rut and do not have a broad view.

Finally, a generally criticized characteristic of bureaucracy is the tendency of persons and organizational units to increase their own importance. "The inherent tendency of bureaucracy to expand" is one of the most common complaints directed at government.[6] This, of course, is an almost universal human tendency. Individuals cherish an increase in status; chambers of commerce seek to make "the biggest little town in America" a little bigger; a corporate management is looked upon with suspicion of inefficiency if it is unable to report that this year the company is larger or did more business than last, particularly if there has not been a general decline in the level of trade.

This tendency is recognized by corporation officials as operative within their enterprises. They complain that executives are too anxious to appear to have an individually outstanding record even though it may be at the expense of the corporation as a whole. Illustrative are these comments:

> The executive personnel has the short view. Their own achievement is all that counts, not the long-time corporation record. For example, one executive set up a hundred new dealers in order to show an 8-percent increase in sales even though it was ruinous to the established agencies.

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[5] A rather extensive literature has been erected upon the base of some limited experimentation along this line at Western Electric's Hawthorne plant. For a summary, see Luther Gulick and L. Urwick, editors, Papers on the Science of Administration (New York: Columbia University Press, 1937), ch. VII.

[6] Friedrich and Cole point out that "under certain conditions, a bureaucracy shows no such tendency at all (post-war France, on the whole, for example)," op. cit., p. 18.

A manager knows he will move on in 2 to 5 years. Therefore, he wants to squeeze everything out in profits instead of planning a long-term program.

It is apparent that the evils of bureaucracy, as evidenced by unresponsiveness, excessive internal legalism, maladjustment of working parts, low morale, and the tendency of persons and organizations to enhance their importance, are not confined to any particular class of human endeavor. Bureaucracy seems rather to inhere in large organizations. Business as well as government must use essentially the same human raw material to operate, and it is, therefore, subject to the same bureaucratic forces which take their administrative tolls. It is apparent, however, that some business concerns are more unfortunately bureaucratic than others, just as are some departments of government.

We need, therefore, to examine the causes of the objectionable features of bureaucracy, together with the administrative remedies which are available. For this purpose, the causes of bureaucracy may be roughly classified as structural and personnel, though it must be recognized that the division is chiefly one of convenience.

CHAPTER V

STRUCTURAL CAUSES OF BUREAUCRACY

The broadest structural cause of bureaucracy, whether in business or in government, is the tremendous size of the organization. Thus, with capital or appropriations measured in hundreds of millions and in billions of dollars, and personnel in tens and hundreds of thousands, it is difficult to avoid the obtrusion of the objectionable features of bureaucracy. For a clearer analysis, and limiting our discussion chiefly to the matter of bureaucracy in business, we must break this broad structural cause into its smaller components.

The first of these constituent causes is the separation of ownership and control in the large corporations. Dennison and Galbraith comment: "We hazard the guess that ossification of the corporate bureaucracy, favoritism, nepotism, and inadequate personnel control become more serious when the ownership interest (which pays the bill) is weak or without voice in control.[1] Our observations tend to substantiate this guess. There is an almost universal tendency for human beings to fall into a rut unless there is some stimulation present. The demand for efficiency by an articulate owner constitutes one type of such pressure which helps to force management out of its lethargy, though of course there are other pressures which act with similar effect. We have already noted the extent to which ownership has become diffused in the large corporation. As a result, so long as dividend payments are somewhere near being satisfactory, the owners will not put pressure upon management to reduce administrative costs. A natural result is for bureaucratic wastes to increase, particularly where earnings can be readily maintained in spite of this drain.

A second structural cause of bureaucracy is the diffusion of authority in some enterprises. Regulatory and operative officials of railroads, for example, agree in interviews that this is an important cause of the ill effects of bureaucracy in this particular field. The management is limited in the extent of its control in administrative matters, and hence unity of command is lost. The Interstate Commerce Commission lays down rather elaborate rules of accounting procedure, passes on extensions and withdrawals of facilities, enters into the fixing of rates, supervises reorganizations and other changes in capital structure—in short, has much to do with the management of the railroads. The banks, insurance companies, and other sources of capital are particularly concerned with management during periods such as the railroads have recently been passing through. The strong labor unions supply rigid wage and seniority rules and enter into personnel administration in many of its aspects. In a given administrative situation, then, there may be several separate and independent entities each having a degree of authority. One may desire one course of action, the other some-

[1] Dennison and Galbraith, op. cit., p. 74.

thing different, or an affected employee may know that he can play one group off against its rival. The result is confusion, inaction, and the perpetuation of administrative defects.

The railroads, of course, are not alone in having a divided administrative authority, for a somewhat similar picture is presented by the utilities and by many of the industrials. This merely illustrates one of the ever-present dilemmas which accompany change. As responsibility for and limits upon administrative actions are extended—in a sense, as trusteeship is made more effective—the undesirable elements of bureaucracy may also unfortunately increase. The object should be to establish the requisite degree of public control and at the same time to maintain administrative efficiency.

Furthermore, the diffusion of authority is not confined to the distribution of powers between the administrative hierarchy and various outside groups. It also exists, according to the testimony of executives in interviews, within the hierarchy itself of many corporations. Thus, for example, when department heads are on the board they are in a sense both equal or superior and at the same time inferior to the president or the chairman. This, it has been said, has a diffusive effect on authority. Matters which concern a department are taken up at the board meeting, and the department head, who may be in disagreement with the executive head of the company on how they should be handled, may not only state his case but has equal voting power with the top executive in determining the final decision. A somewhat analogous situation would exist if the departmental and bureau officials in the Federal Government, who now have contact with legislative committees and sometimes give advice contrary to that of their superiors, were not only able to influence legislation and contribute to divisive bureaucracy as much as they do now, but were actually allowed to vote as members of the particular legislative committees concerned.

In addition, the officer board may present an impediment to administrative unity in still another way. Thus, some executives report that the officer members, on leaving the board meetings, act before the policy adopted or the decision made in the meeting can be adequately translated into a unified series of orders. Or again, headquarters staff men issue instructions to line executives, who thus are placed in the position of taking orders from a number of persons. When there is no central clearance, these sometimes conflict and confusion results. "We have lots of fights with men in the field," one such staff man remarks.

Of course if all action had to clear through strictly proper hierarchical channels, in a large enterprise the steps would be numerous and complicated and extended delays would ensue. On the other hand, if short cuts are to be taken, such as the direct dealings of staff and line men mentioned above, confusion and conflicts are equally likely to occur. This is another of the many managerial situations which illustrates the proposition that bureaucracy is inherent in large-scale enterprise. Both horns of the dilemma are labeled with that word.

An important stone in the logical edifice which Frederick Taylor built was that the worker at the bottom of the hierarchy should have as superiors a number of so-called functional foremen, each giving instructions in his particular field. In actual practice, however, this organizational device never received wide adoption in American

industry. Even though Taylor conceived of a planning and coordinating staff at headquarters which would supply unity and direction, the system engendered too much confusion.[2]

Nevertheless, even though the functional-foremen part of Taylor's plan was found unworkable at the bottom levels, something closely resembling it in the upper levels has sprung up. As a necessary compromise between specialization and order with unity, functional executives advise subordinate line officials in the realms of their specialties. This works very well so long as everyone recognizes that advice is what is being issued. But the dividing line between advice and command is so dim as to be frequently indistinguishable in practice.[3] In fact, no such line can be drawn. When what seem to be orders to those concerned come from several sources, the executives find themselves in much the same state of confusion as do the workers under functional foremen. The testimony of the executives of large corporations indicates that this condition does exist in parts of their domains, although it may be excused, perhaps, as an unfortunate concomitant to necessary administrative informality.

A third cause of bureaucracy which results from size is the formalization of interpersonal relationships. In a very small enterprise, face-to-face contacts and informality are characteristic. Long before the level of the giant corporation is reached, however, the superior officers are several steps removed from the laborers and foremen. No longer is it possible for the boss to say personally to his workers, "This is what I want done and the way I want it done," nor can the workers tell the boss what they think would be better objectives or methods. The number of persons concerned in a large enterprise precludes such simple arrangements. Rather, a hierarchy must be set up and rules established in order that the efforts of thousands of employees may be directed toward common objectives.

Perhaps it will be considered possible to maintain the interpersonal characteristics of a small enterprise in a large one. This might be so if each small subdivision were run as a separate business. Such a procedure, however, would sacrifice much of the advantage of the large enterprise. Specialization among departments would have to be eliminated and its benefits lost. Coordination of the work of the various groups of workers would be difficult. In actuality, therefore, not only is a hierarchy necessary in a large enterprise, but also a set of rules whereby the members of the hierarchy must act.

The extent to which formal rule-making is carried in the large enterprises varies widely. Some companies have been casual about it, but others have worked out elaborate and detailed sets of instructions which are published and sent to all officers who are concerned. In Armour & Co., for example, a loose-leaf book of regulations is issued to all branches and is revised from time to time. Similarly, in the American Telephone & Telegraph Co. the "Bell Bible," as it is familiarly known, is a comprehensive collection of the rules and standards which apply to particular parts of the system. The regulations covering a single department in this company constitute an impressive pair of loose-leaf volumes. Those of immediate con-

[2] For a good review of Taylorism, see H. S. Person, editor, Scientific Management in American Industry (New York: Harper, 1929).

[3] For an excellent discussion of the actual nature of authority see Chester I. Barnard, The Functions of the Executive (Cambridge, Mass.: Harvard University Press, 1938), ch. VII. Barnard is president of the New Jersey Bell Telephone Co.

cern to, say, a telephone installer are also issued in a loose-leaf booklet of pocket size. The instructions themselves are very explicit, setting forth in detail the exact methods to be followed and the extent to which a person should use his own judgment. In other corporations which did not have so complete a system of procedures applying to standards, methods, and supervisory practices, the executives expressed the belief that such a body of rules should be developed and adopted, particularly for use at the lower levels.

The control systems which all of the large corporations use must include uniformity in reporting in order to make that control effective. When results are judged only on the basis of net profits for particular subdivisions, reporting-procedure rules are simple. In the Du Pont Corp., for example, the executive committee determines what percentage on the investment each subsidiary or operating department should make, and the operating head is then given considerable leeway in devising administrative methods whereby the quota may be reached. If it is missed, he will have some explaining to do, but otherwise he will be relatively free in administrative matters.[4] When detailed control over expenses, sales, and the like, is attempted, on the other hand, the reporting rules and procedures must be more extensive. One item of expense must mean the same thing throughout the enterprise. This process is still further refined when, as in the Bell System, control items extend to such things as the percentage of errors in handling telephone calls. Just what constitutes an error, for example, must be carefully defined.

Thus, in all of the large corporations rules of a more or less explicit nature must be utilized. But they formalize inter-personal relationships and thus contribute to the ills of bureaucracy through the decline of the human touch.

The use of rules can, of course, be carried too far. "The temptation is to hide personal responsibility behind rules and regulations."[5] Moreover, the attempt to cover every conceivable situation by means of a definite rule for the sake of uniformity can result in such a maze of instructions that they are a hindrance rather than a help. John Lee has aptly said, "It is possible so to refine the sense of justice as to negative positive action."[6] Henry Dennison expresses the same thing in another way: "Attempting to manage without rules is doing by hand what might be better done by machine; attempting to manage entirely through rules—to let rules manage for you—is to overmechanize and to suffer from rigidity."[7]

It is difficult to determine whether, from the standpoint of internal administration and considering the companies' needs, the use of rules in the giant corporations has been overextended or somewhat neglected.

Some executives feel, for example, that rules have been carried too far;[8] others that they have not been developed far enough. From the extensive use of rules as administrative tools it is an easy step blindly to follow or to use them as an excuse for decisions which show

[4] See "Du Pont: A Management and Its Philosophy," Fortune, X (December 1934), pp. 86ff.

[5] John Lee, "The Parallels Between Industrial Administration and Public Administration," Public Administration, IV (1929), pp. 216, 221.

[6] Ibid., p. 222.

[7] Henry S. Dennison, "Who Can Hire Management?" Bulletin of the Taylor Society, IX (June 1924), p. 101.

[8] One official claimed that his outstanding accomplishment as executive officer was that of reducing the number of written regulations. As he expressed it, "You can't expect a good man to show his abilities unless he is given freedom to put his ideas into operation."

administrative incompetence. This emphasis on legality is apparent in Government, but its obtrusion in private business is equally clear. This is illustrated by the fact that the top executives of some corporations repeatedly have to emphasize that results are more desirable than blind conformity to rules. It should be remembered, however, that in the case of regulated enterprises, such as the railroads and the utilities, legality may be as or even more important than results in particular cases.

From the standpoint of the customer or the public, corporate rules—or "company policies" as they are sometimes called—may seem bureaucratic in the extreme. Since methods and practices are determined by administrators, it is natural that they should reflect administrative rather than public convenience. This is generally true except where a sufficiently strong counter-force can be applied to make the self-interest of the administrators synonymous with public convenience.

Corporation officials themselves mention examples where rules are a hindrance. A former official of one giant corporation cites this example: The corporation had contracted with another to supply equipment. Some of it was unsatisfactory and the management of Corporation A decided to use superior equipment which they could get for less money. Corporation B threatened to sue, but one of the vice presidents came around to Corporation A's viewpoint and told them they could use the superior equipment. A second vice president was, however, concerned in the matter and he protested to his colleague and an official of Corporation A: "You can't do that. We have our policies and they won't permit it." The other vice president countered with: "But this is my field and I stick by what I told them." The reply which closed the conversation was, "I don't believe in bringing out our family quarrels into the open. We'll consider and let you know." After some delay, however, Corporation A's viewpoint was sustained. Ordinarily customers could expand ad infinitum the list of irritations resulting from rules.

But merely because rules are irritating or rigidifying does not necessarily mean that they should be abandoned. They cannot be dispensed with and unity of action retained. The administrative problem is carefully to weigh the merits and demerits of particular regulations and to adopt only those whose benefits are clear. A corporation official aptly warns: "It is easy to go too far in rule-making." Even a well-conceived body of instructions will invariably have some ill effects. It illustrates what we have already pointed out: you can't take all of the bad effects of bureaucracy out of the necessary bureaucratic structure.

Closely allied to the system of rules, written and unwritten, which pervades the large corporation is the aura of institutionalism which surrounds many of these enterprises. In a complaint on the dearth of leadership, for example, a prominent member of the Taylor Society has said:

> The nature of our industrial institutions has become such as to render almost impossible the emergence from that source of leadership with a collective point of view. When a young man enters into the service of a corporation he enters into a bureaucracy which has institutional ideals, aims, and purposes; and a powerful though perhaps unwritten institutional code.
>
> Generally he realizes little opportunity for individuality and self-expression except insofar as these conform strictly to the institutional aims and bureaucratic

code. The consequence is that few individuals in the service of corporations can, while they are still young and plastic, break through the restrictive shell and stand forth as leaders unrestrained by particular interests.[9]

In a somewhat similar vein, a leading utility executive tells of his impressions when he first entered a giant corporation:

The constantly expressed phrases—"The good of the organization," "The service as a whole" * * * seemed to be the real basis for what I at first felt to be repression of the individual who was becoming less and less significant. This repression was evident not so much in specific directions concerning work to be done as by inhibitions and prohibitions arising out of the intangible barriers of departments, grades and ranks, policies, appropriations, laws, prejudices and economic limitations of consumers. * * *

I was in danger either of falling into a complete lethargy from my inability to reconcile two apparently contradictory (individualistic and collectivistic) states of affairs; or of attempting to treat myself either as a slightly conscious and unimportant cog in a gigantic machine, or as an anarchist determined to assert my individuality in destructive action. You can see all about you men and women whose escape from the dilemma * * * has been through one of the three doors I have described. * * *

I happily escaped from the dilemma through the fourth door which was that of directing my individual efforts not only in conformance with, but in furtherance of, the objectives of the organization.[10]

Individualism in the sense of freedom of action does not exist to any appreciable extent in the large corporation. For the few who are in control, such a state may obtain; but for the thousands of workers, their fortune is to adapt their individualism to the demands of the organization. "Our company is no place for an individualist," one executive of a giant corporation has succinctly said. Although the institutional needs of the corporate bureaucracy demand this, its effect is often to deaden initiative and to lose potentially valuable executive material.

Another cause of bureaucratic confusion and indecision is the often inadequate definition of the scope of authority and responsibility among the various departments and executives. There is almost universal agreement among administrative theorists that the scope of authority and responsibility should be rather concretely outlined, even though they recognize that the rule is more often broken than obeyed. Among corporation executives there is a similar agreement as far as the lower levels of the administrative hierarchy are concerned. In regard to the upper levels, however, there is a sharp difference of opinion among the practitioners. For one group this statement is typical: "At the highest level, organization is merely a matter of common sense, good will, and informal relationships. There can be no hard and fast organization and lines of control at the top." But an executive in the opposing camp counters with: "You can't do a job until you know what it is. The attitude that lines of communication and authority become informal the nearer the top you get, and can be precisely defined only at the lower limits, is due to laziness and inertia. The executive fights like a steer against defining his own job. The very men who resist are almost invariably the ones who need such definition most."

At the lower levels of most large corporate structures job definition has made considerable progress, whereas at the top flights little or nothing has been done, with a few notable exceptions. Indefiniteness may cause delays and jealousies, whereas, an excess of rigidity almost

[9] H. S. Person, "The Call for Leadership," Bulletin of the Taylor Society, XVIII (June 1935), p. 41.
[10] Chester I. Barnard, Collectivism and Individualism in Industrial Management (New York: American Telephone & Telegraph Co., 1934), pp. 4–5.

certainly causes inefficiencies. Either extreme is objectionable. The proper balance is the goal.

A sixth structural cause of bureacracy of which executives complain is the difficulty of communication and integration because of the number of hierarchical and interdepartmental divisions, and the separatism and insulation which exists among them. A number of executives list this as one of the principal or even the principal weakness of big business.

One official, for example, has said, "The larger an organization becomes, the more difficult it is for all concerned to obtain information. No one can see everything, know everything, or be acquainted with everyone." Some of the giant corporations have eight, ten, or even more steps in the hierarchy. Effectively to cross all of these bridges with plans or suggestions is a major problem. For one thing, ideas change as they pass from one mind to another; their final interpretation may be something quite different from the original proposal, and they may even be completely lost in the process. The possible ineffectiveness of the resulting action, if any, on the many fronts concerned is obvious. Furthermore, taking the required number of steps is time-consuming, and decisions may in the end be so far removed from the point of action as to be useless.[11] "When the important decisions are infrequent, and the necessity for a quick decision is less urgent, the large firm can play its part more efficiently."[12] When more rapid action is required, however, the large enterprise often reveals its bureaucratic inflexibility and finds itself unable to act with dispatch. And even though a procedure for speedily handling emergencies may be developed, routine matters necessarily take longer in the large than in the small enterprise, despite the best administrative methods.

In the large enterprise the advantages of functional specialization are apparent. Because of the scope of the giant corporation it may be profitable to have a number of specialists devoting full time to small sections of the immense administrative and technical problems of big business. This, however, results in bureaucratic rigidification in two principal ways. In the first place, the multiplication of specialists means that at a given level of the hierarchy more persons are responsible to one executive than is the case in smaller enterprises. Just what may be the optimum number of immediate subordinates which one executive can effectively handle is difficult to say, since so much depends upon the executive and upon the type of work which is being done. There are, however, outside limits which are often exceeded. Other things being equal, the larger the number of immediate subordinates, the more difficult the problem of communication and integration. It has been demonstrated that with an arithmetic increase in the number of such subordinates, the inter-personal relationships—and necessary lines of communication—increase in geometric ratio.[13] The result is that many executives find their effective span of control exceeded, with resulting confusion and loss of integration.[14]

[11] John H. Williams makes this last point. See his "Is There an Optimum Size of Organization?". Bulletin of the Taylor Society, XV (February 1930), p. 22.

[12] E. A. G. Robinson, The Structure of Competitive Industry (New York: Harcourt, Brace & Co. 1932), p. 49.

[13] See V. A. Graicunas, "Relationship in Organization," in Gulick and Urwick, editors, op. cit., ch. X.

[14] For a more comprehensive presentation of the problem of the span of control, see Marshall E. Dimock, "The Span of Control in the Federal Government," Society for the Advancement of Management Journal, III (January 1938), pp. 22–28.

Secondly, the development of functionalism and specialization also makes communication more difficult because of the loss of a common language and understanding. Each specialist becomes engrossed in his own field and knows progressively less of the problems of his colleagues in the enterprise. Inter-departmental insulation thus develops. Moreover, with well-developed specialization among his subordinates an executive finds it difficult to coordinate those directly responsible to him. He cannot be expected to know all about each of the specialties and so he cannot see all of the ways in which the affect each other. The head of one enterprise sums it up in this way: "A grave defect of the large-scale concern is that the executives become too specialized. Each man has his own department and he loses perspective. The business is segmented. The top executive loses touch."

Thus, functionalism has bureaucratic results. Its advantages, however, are so great that it is not possible to seek a return to simple organization. "The functional system is inevitable, but it is the work of human beings to safeguard humanity against many ills which seem to accompany movements apparently inevitable." [15]

In summary, we have mentioned six groups of structural forces which stimulate the obtrusion of bureaucracy in big business. These are the separation of ownership and control, the diffusion of authority in and over an enterprise, the formalization of rules, the growth of corporate institutionalism, the lax definition of authority and responsibility, and difficulties of communication and integration. Not all of these are of equal importance in all large enterprises, but all affect many of the corporate giants.

These structural factors, however, are only some of the causes of bureaucracy in business. What we have called the personnel factors are fully as important. To an examination of these elements we may now turn.

[15] John Lee, "The Pros and Cons of Functionalization," Bulletin of the Taylor Society, XIV (June 1929) 114.

CHAPTER VI

PERSONNEL CAUSES OF BUREAUCRACY

Ineffective leadership.—Among the personnel causes of bureaucracy of which business executives and students of administration most often complain is the lack of competent, effective leadership. As the head of one enterprise has remarked, "there aren't enough first-class executives to go around. They are almost as rare as inventors and first-class research men, so unusual a combination of qualities—plus an ounce of 'divine spark'—must they possess." Herbert Emmerich has criticized the popular idea that "a good executive is a 'no man' entirely surrounded by 'yes men.'" "Executive management," he has said, "is a constant process of evoking from the human beings who comprise an organization their best contributions toward its work. This cannot be accomplished in a negative atmosphere. The top executive of the future will bend most of his efforts toward discovery and release of the creative forces of his organization, not to their suppression."[1]

The necessary executive traits are by no means few or simple. In one instance they have been summarized thus:

> The successful leader is characterized by a reasonably high degree of such personality traits as initiative, enthusiasm, imagination, knowledge, originality, persistence, speed of decision, and purpose. His relations with his followers are characterized by sympathy, tact, patience, faith, prestige, and ascendance-submission.[2]

Ordway Tead has written extensively and perceptively on the subject of leadership. Among the qualifications which he sets forth are physical and nervous energy, enthusiasm, an adequate technical knowledge or skill in relation to the project in question, mental alertness, imagination or the ability to work with the data of past experience in newly conceived combinations, knowledge of human nature, a belief in the spontaneous and self-generating powers of individuals in groups if they are given a chance to exercise them (or more simply, faith in people), courage, persistence, initiative, tact, patience, self-confidence, a sense of humor, and purposiveness. Moreover, he stresses:

> Creative leadership can best manifest itself only under those corporate conditions wherein a consistent way and in terms of practical working devices, and not merely in verbalisms, the corporation is demonstrating clearly to its workers that it desires to consider them as partners in a group enterprise and not merely as agents for the piling up of excessive profits for absentee owners. * * * The leader, it must be emphasized, is not a beguiler, a bully, a seducer, or a hypnotist in respect to the purposes of those whom he leads. Only as he is a teacher and inspires and is fully envisaging broader and broader aims can his appeal remain effective.[3]

[1] Herbert Emmerich, "Some Folklore of Executive Management, Public Management," XX (September 1938), pp. 264–267.

[2] H. L. Smith and L. M. Krueger, A Brief Summary of Literature on Leadership (Bloomington, Ind.: University of Indiana, School of Education, 1933), p. 38.

[3] Ordway Tead, "The Nature and Uses of Creative Leadership," Bulletin of the Taylor Society, XII (June 1927), p. 394.

An executive of one of the country's largest enterprises has pointed out that the power of the president of that company was in fact not nearly so great as was generally supposed. "If he can't keep the confidence and esteem of his vice presidents and the presidents of the subsidiaries he will be ineffectual." Just as the head of a company is dependent upon others in the formulation of his decisions, so also is he dependent in their execution.

The field of leadership as a whole is too broad a subject to be discussed here in detail. We may, however, mention briefly some of its elements as they bear on the direction of the large corporation.

The importance of leadership is universally acknowledged. With almost equal unanimity corporation officials testify to the difficulties which attend the training and promotion of leaders to fill positions where their influence is needed and where it will be effective. Although the degree to which the executives of large corporations inspire their subordinates is too subjective for extended consideration we may nevertheless mention some of the more important aspects of the matter. We have evidence, for example, that the leaders, and particularly the chief executives, set the tone of the whole enterprise. It is, therefore, important that this tone, with its direct effect on morale, be not characterized by the harmful elements of bureaucracy which we have indicated.

For our present purposes the discussion of the relation of executive leadership to bureaucracy may be confined to five general requirements. These are that the executive not be too old upon appointment; that he possess a broad outlook; that he reach office primarily on the basis of merit; that he remain in office long enough to be effective but not so long as to become senile; and that positions of leadership be attractive to potential leaders. It is recognized that these are capable of broad interpretation; we may, however, note tendencies in each of them.

A leading figure in the field of industrial management maintains: "It is hardly to be gainsaid that with the steadily increasing age at which executives reach the top rank of president or chairman of the board, they find themselves physically, as well as intellectually less able than under former conditions of corporative simplicity to cope with the question of future progress and growth." [4] It cannot be flatly said, of course, that advanced chronological age means a corresponding loss in mental resiliency. Daniel Willard, president of the Baltimore & Ohio Railroad, and the late Justice Holmes serve amply as refuting examples. There can be no doubt, however, that there is a general tendency in this direction—that, in general, resiliency is lost with age. Because of this, summary figures on age have meaning in relation to corporate leadership.

Table X presents some biographical data on the heads of 35 of the Nation's largest companies. The size of the sample is small, but it should at least indicate some of the tendencies.

For this group as a whole, the chief executives were appointed at an average age of about 50 years. By 1939 they were approximately 61 years old, having served an average of about 11 years. As might be expected there is much variation among the companies. For example, in the cases of three of the industrials and two of the utilities, the chief executives were chosen at the age of 40 or less.

[4] Harry A. Hopf, in the Georgetown Law Journal, XXIV (1938), p. 1067.

At the other extreme, one railroad and one industrial had heads who were more than 64 years old when appointed. Obviously the term of office for these older men must be relatively short.[5] In general, it may be said that with an average age of 50 for the group as a whole, a number of these executives were advanced to top positions when they were somewhat beyond their prime.

TABLE X.—*Executive heads of 35 giant corporations, 1939* [1]

Corporate group	Age on appointment to present position		Age in 1939		Years with company		Years in particular field of business [2]		Source, in percent [3]	
									Promotion from within company	Brought from outside company
Industrials	[4] 49.3	(49.6)	61.3	(60.6)	36.3	(30.7)	37.3	(34.2)	90	10
Utilities	46.3	(45.0)	55.0	(57.0)	20.0	(19.4)	30.5	(31.1)	70	30
Railroads	55.0	(55.0)	62.0	(64.2)	38.0	(34.9)	40.0	(42.1)	75	[5] 25
All	50.5	(49.9)	60.7	(60.6)	36.0	(29.3)	37.3	(35.4)	80	20

[1] The group includes 19 of the 20 largest industrials (data was unavailable on 1), the 8 largest utilities, and the 8 largest railroads. With the 1 exception, this is the same group of corporations whose directorships were analyzed on p. 24 ff., supra. Data on 2 industrials and 1 utility are incomplete; averages in the affected categories are derived from the remaining number.

[2] Figures are very rough because the point of entry into a particular field is difficult to define.

[3] Percentages are approximate.

[4] Median values used are the arithmetical averages of the central 2 or 3 items and are shown without parentheses; arithmetical means are shown in parentheses. Where 1 man was not clearly the executive head of a company the average of the combination of men which appeared to hold that position is used. The titles of the executive heads vary. Usually it is the chairman or the president or those two combined. In 1 case, however, it was the executive vice president, though he has been subsequently made president. The men are those that held the top positions when Moody's Annuals for 1939 went to press. Changes since then are not incorporated in this table.

[5] The 2 heads of railroads included here were brought from the presidencies of other, smaller railroads.

Age upon appointment is probably more important than that at a given date because the executive who has served for some time has the advantage of experience in the job to balance against the handicaps of his advancing years. Current age, however, is interesting. For example, the executives as a group were approximately 61 years old in 1939. Again there were rather wide variations. Only 1 was younger than 45 and 3 younger than 50; at the other extreme 4 were 70 or more. Half were 60.7 years old (the median) or more; 10 were 65 or over. Since the retirement age in many companies is 65 this indicates that a fairly large proportion had passed the point which, according to many corporation officials, should mark the cessation of active dominant executive direction, unless rather exceptional circumstances intervene.

The age tendencies are not at all alike among the 3 corporate groups which were examined. The picture for the industrials, for example, is quite similar to that of the 35 corporations considered as a whole. The averages and the dispersions are about the same for both. The utilities and the railroads, however, present a different picture. Thus, the largest utilities have chief executives who were appointed when they were 4 or 5 years younger than was usual for the 35 corporations, and their present age is likewise about 4 years below that of the group average.

[5] One of these was retired late in 1939 after having served for 4 years. The other was appointed more recently and is still in office.

The railroads, on the other hand, are run by substantially older men. The usual appointment age here is some 5 years higher than for all of the 35 corporations; the age in 1939 was 1.3 to 3.6 years above the average for the larger group, depending upon whether the median or the arithmetic mean is considered. The belief that bureaucracy in railroad management is partly due to the relatively advanced years of railroad executives seems to be substantiated by these data. The unprogressiveness of railroad management in service, pricing, and operational policies may well be due to some extent to the decreased mental and physical vigor of those at the top, although doubtless there is more than this in the picture as a whole.

A question which should be raised, however, is how the relative youth of the top executives of the utilities affects bureaucracy in those companies compared to its prevalence in the railroads. Although we are not prepared to give a complete answer, it does appear that the unprogressiveness and unaggressiveness of the utilities are more in their pricing and other marketing policies and practices than in their operational and administrative aspects; while among the railroads the ills of bureaucracy extend to these latter activities as well as the former.

There is no group of positions in the Federal Government which strictly compares with the presidencies of the giant corporations. The nature and variety of the tasks of some of the top governmental officials are both different and more complex than those faced by corporation executives. There is no other job in the Nation, for example, which can compare in variety of problems with that of the Presidency. Much more than administrative ability is required if the position is properly filled. The President must be in tune with the voters of the Nation—who are more effective than stockholders because a choice in leadership is offered them—as well as plan for their welfare and for the Nation's place in the world. The departmental heads, in addition to their administrative tasks, assist the President in his political and policy-determining functions and are in turn aided by their immediate subordinates. There is a fairly rapid turn-over at each of these three levels. One must drop to the level of the bureau chief, therefore, to find men whose work parallels that of the corporation president, though they must work under the political heads we have mentioned. In speaking of these men Lewis Meriam comments:

> Governmental activities are such that these permanent offices often have the developmental, expansive side which in private enterprise may be the strength of the top executives. One may indeed raise the question whether a bureau chief with his upper civil servant assistants is not more comparable with a corporation executive than is the President of the United States.[6]

Despite the limitations, however, we may make some rough comparisons of these upper-level groups. Tables XI to XIV present some summary age data on the Presidency and the three next subordinate levels in Federal administration.

Table XI shows that on the average our last eight Presidents have assumed office at the age of little more than 54 years.

[6] L. Meriam and L. F. Schmeckebier, Reorganization of the National Government (Washington: Brookings Institution, 1939), p. 75. It should be remembered, however, that Meriam is a believer in the decentralized type of Federal administration and thus may have a tendency to overemphasize the bureaus.

TABLE XI.—*8 most recent Presidents of the United States*

	Arithmetic mean	Median [1]
Age at assumption of office	54.1	54.5
Length of term [2]	5.4	5.5
Years in governmental positions prior to assumption of office	14.9	16.0
Source:		
State Governor .... percent	37.5	------
Succeeded from Vice Presidency .... do	25	------
Head of a Federal department .... do	25	------
Senator .... do	12.5	------

[1] The median used here is the average of the 2 central items.
[2] Includes 7 years of the term of Franklin D. Roosevelt.

This is about 4 years older than the usual age at which the executive heads of the 35 giant corporations assumed their top positions. It is about the same as the average for the railroad group. The brevity of Presidential tenure, however, makes the average age at which a President leaves office about equal to the average current age of the corporation presidents. This current age may be considered as lying somewhere near the midpoint of the composite terms of office; thus the average retirement age for corporation executives is several years beyond this. The average age of Presidents, then, midway in their terms of office, is slightly below the corresponding average for the top executives of the largest corporations.

The 15 governmental executives who head the 10 Federal departments and 5 other large administrative units were appointed to office at almost the same age as the average for the heads of corporations. This is shown in table XII. Their current ages, however, are about 5 years below the corporation average and are also slightly below the average of the utility group.

TABLE XII.—*Executive heads of the 10 departments and 5 other large agencies of the Federal Government, December 1939* [1]

	Arithmetic mean	Median [2]
Age at appointment	50.7	48.7
Current age	54.9	51.0
Years in governmental positions	15.3	8.7
Source:		
Promotions from within the Federal administration [3] .... percent	47	------
Other governmental or political positions .... do	40	------
Nonpolitical positions .... do	13	------

[1] The five agencies included are: Federal Loan Agency, Federal Security Agency, Federal Works Agency, Government Printing Office, and Veterans' Administration.
[2] The median figure used is the average of the central 3 items.
[3] For example, 3 secretaries were formerly under secretary or assistant secretaries.

The under secretaries and assistant secretaries over a period of years have followed this general pattern at a slightly younger level. Thus, at the time of appointment they have been from 1 to 4 years younger than the secretaries we have examined. Their age levels at any given time, of course, would naturally lie correspondingly below those of the secretaries because their terms of office are roughly comparable. A summary of the data concerning this group is given in table XIII.

TABLE XIII.—*Under secretaries and assistant secretaries* [1]

	Arithmetic mean	Median
Age at appointment	46.9	47.5
Average tenure (months)	51.4	34.5

[1] Adapted from A. W. Macmahon and J. D. Millett, Federal Administrators (New York: Columbia University Press, 1939), p. 296. The items given here are averages of the averages for past and present incumbents of the 24 specific posts listed on the page indicated.

At the bureau level this trend toward younger men is at least temporarily halted, although the age level still lies below that of the corporation executives. This is briefly indicated in table XIV.

TABLE XIV.—*62 bureau heads* [1]

Average age at appointment	48
Average age in 1938	53.6
Source:	Percent
Recruited under formal merit systems	48
Unrestricted:	
Promoted from within national administration	23
Taken from state or local service, or from cognate semipublic background	19
Political recruitment	10

[1] Adapted from A. W. Macmahon and J. D. Millett, Federal Administrators (New York: Columbia University Press, 1939), p. 454.

The 62 bureau chiefs in office in 1938 were appointed at an average age of 48, and their current age at that date was 53.6 years. This is almost the same as the ages which obtained in the affected departments 12 years earlier, which indicates a rather settled policy in regard to the ages of bureau chiefs.[7] The corporation executives were appointed to their positions when they were about 2 years older than were the bureau chiefs, and their current age is about 7 years beyond that of the Government officials.

Insofar as direct comparisons are possible, the following may be said in summary: the appointment age of the top officials of the Nation's largest corporations is about the same or slightly above that of the top layers of Government officials. The average current age, however, is considerably higher than that of Government officials. To the extent that the undesirable aspects of bureaucracy are due to the advanced years of some of the top executives, it is apparent that this cause exists in the large corporation to at least the same degree if not more than it does in Government.

The second aspect of executive leadership is broadness of outlook. In even a moderately large corporation the administrative problems are many and diverse. The executive must be capable of harmonizing a multitude of conflicting forces. In the giant corporation, therefore, the ability to see things broadly and in relation is correspondingly more essential. Since most of the heads of the largest companies are promoted from within [8] the question should be raised as to whether broad-gage executives can readily be developed in such enterprises.

[7] Cf. A. W. Macmahon and J. D. Millett, Federal Administrators (New York: Columbia University Press, 1939), p. 454.
[8] See Table X.

A number of executives believe that the large corporation develops outstanding executives with considerable difficulty. The head of one company went so far as to say that "large corporations do not produce great executives. The men tend to become too specialized. The man in a smaller organization gets to know the business as a whole at an earlier age." Another phrases the problem in this way: "Specialization results in a dearth of top executives. You can't find men to integrate because they themselves aren't integrated. I know more good all-around business men in small concerns than I do in big corporations." Or again, "As activities become more specialized and routinized it becomes more difficult to develop ability in the ranks. * * * It may not be safe for us to rely upon securing a sufficient number from the ranks who will qualify for executive leadership." [9]

The benefits of specialization, of course, constitute one of the principal advantages of the large corporation and can ill be sacrificed. Although some top executives demonstrate that specialization is not an insuperable barrier in the development of leaders, nevertheless it remains an impediment in the process of such development and is, therefore, a contributing cause of bureaucracy in big business.

In the Federal Government the bureau chiefs are probably specialized to about the same degree as the corporation executives. Among the higher political heads, however, there is a characteristically broader experience and outlook. It is the business of the politician to compose differences and to recognize the implications of particular policies over a broad realm. To the extent, then, that specialization is a cause of bureaucracy, the large corporation suffers as much as and perhaps more than Government.

The third general requirement for good leadership is that the executive shall have reached his position on the basis of merit. The degree to which merit now plays a part in appointments is difficult to determine. With the diffusion of ownership, which is characteristic of the large corporation, there is a corresponding decline in the practice of placing the chief owner or his son or some other relative in the higher executive positions. Although the propensity to "play ball" with the existing control is doubless a factor in the selection of executives, this relative disappearance of inheritance as a selector opens the way for an emphasis on merit per se and it is possible that this will be the future trend. Inheritance is too unreliable a determinant for us to weep over its eclipse.

Although merit has doubtless played an increasingly important part in the selection of the top executives of large corporations, one nevertheless hears the complaint, from other than those who may be expected to be prejudiced, that seniority has been too much emphasized. This is particularly true, for example, among the railroads and doubtless contributes to the relatively high age at which men in this field are appointed to top positions. The idea of promotion by seniority permeates the railroads all the way down the hierarchy, where men are apt to think more in terms of the time in their records than in how effectively that time has been spent.

But promotion by seniority is not confined to the railroads. Some executives feel that the practice is generally characteristic of the large

[9] James O. McKinsey, Organization Problems Under Present Conditions (New York: American Management Association, 1936), General Management Series No. 127, p. 13. The late Mr. McKinsey was chairman of the boards of Marshall Field and Co. and of the American Management Association.

corporation. Moreover, even if it were no more common there than in the small enterprise, the process of reaching the top would take longer because of the greater number of steps in the hierarchy. In any case, it is at least certain that the big companies as a rule do not have an adequate system of executive recruitment. In regard to this lack, Edward R. Stettinius, Jr., for example, believes that a method of inventories should be developed whereby just as exact a record could be kept of executive material as now exists for other materials.[10] Some of the largest companies are now engaged in developing the first stages of rating systems and refined records to assist in uncovering executive talent and in advancing it rapidly enough to be really effective. But such methods are relatively difficult to operate and do not enjoy wide acceptance in big business. On the other hand seniority is so easy a method to apply that in the lack of a better one it is natural that it should be used. Seniority is one of the few things about an executive that can be accurately and objectively determined. Those who are passed over cannot complain that on the basis of selection used they should have been advanced instead. Nevertheless, length of service does not guarantee the requisite qualities of a leader. It is essential, therefore, that other methods of rewarding such devotion be discovered and used so that leadership will not be sacrificed on the altar of convenience and in a way that is of doubtful benefit to employee morale.

Seniority, of course, is also used in public administration as a basis of promotion. We do not, however, have available material to indicate the extent to which this method is employed. Nevertheless, since the average ages of the top officers at the time of appointment, both in government and in private enterprise, are not widely divergent, there is at least an indirect indication that promotion by seniority is no more prevalent in one instance than in the other.

In their study of Federal administrators, Macmahon and Millett make their prime dichotomy of the bases of selection that of a division into political and nonpolitical criteria. Among the bureau chiefs they found that only about 10 percent were examples of primarily political recruitment.[11] The extent to which seniority played a part in the selection of the other 90 percent we are not prepared definitely to say. A general knowledge of civil-service procedure, however, indicates that seniority is clearly a factor in promotion under that system because the experience which a candidate has to his credit is often given substantial weight. On the other hand, since bureau chiefs are appointed at an average age of about 48 and since turn-over of Government employees at the lower levels is generally below that of industry, there is indirect evidence that, comparatively, seniority controls no more and perhaps even less than in large corporations.

In regard to the Assistant Secretaries, Macmahon and Millett cite a number of examples where appointment was clearly on the basis of merit, although on the whole they conclude that "haphazard political considerations have been the outstanding factors" in the selection of these men. They do comment, however, that among them "there has been a marked prevalance of college graduates." [12] The preceding positions of the current departmental Secretaries and the last eight

[10] Edward R. Stettinius, Jr. "The Selection of Executives," Management Review, XXV (November 1936), pp. 332–333.
[11] See table XIV.
[12] Macmahon and Millett, op. cit., pp. 290, 294.

Presidents indicate that the great proportion came from jobs which in relation to their present rank may be classified roughly as analagous to "operating vice president" or "assistant to the president" in corporations.[13] In business these posts are commonly springboards to the top.

On the whole, then, we cannot say that merit for the particular jobs to be done is given any less consideration in government than in business. Politics, of course, plays a part in both. As one executive expressed it: "Politics exists in all large corporations. Whenever there is a change at the top in our company there is a shake-up all along the line." There is much room for improvement in both business and government, and, in each, some of the policies of executive recruitment result in defective leadership and contribute to bureaucracy.

The fourth qualification for leadership is that the executive remain in office long enough to be effective. Just what this term may be is difficult to say. Some executives claim that "a creative man delivers all he has in 3 to 5 years on one job." While this may be true at some of the lower levels of the hierarchy we doubt that it accurately describes the situation at the top. A well-conceived program of action would require 3 to 5 years to be properly developed and put into operation. An even longer period would be required for it to become an integrated part of the enterprise as a whole. Continuity of office is essential to smooth continuity of policy. Our general conclusion, therefore, is that although the exact length of appointment cannot accurately be determined, 10 years is not too long for a capable man to direct an enterprise while even 3 years is too long for a poor one. The problem is to select well and then to allow a sufficient length of time for the executive leader fully to put his ideas into effect.

In general, the top executives of the largest corporations have terms of office that are satisfactorily long. Table X indicates that the present incumbents, on the average, have held office for 10 or 11 years. Since this measure is taken in the midst of their terms we may suppose that the total, on the average, will be somewhat longer. If the sample were entirely representative both as to time, in relation to say, the business cycle, and as to coverage of variation among corporations, the average term would be approximately twice that of the time already served. In spite of such imperfections as the sample undoubtedly has, we may safely suppose, therefore, that the average term is at least 5 years longer than the elapsed part of it, which would indicate a minimum average for top executives of about 15 years. The average term for the railroad executives would be something less than this because of their more advanced age. This assumption is supported by the smaller elapsed time which current railroad executives have served. These men, as shown in table X, have been in office from 7 to 9 years while the average for utility and industrial executives is from 9 to 12 years. Thus, for the group as a whole there appears to be a healthy continuity of office,[14] although individual variations are wide, of course, and some executives remain after senility overtakes them. In general, however, the picture is favorable.

[13] See tables XI and XII.

[14] While some persons believe that a relatively long term of office is an undesirable attribute of bureaucracy we do not subscribe to that notion. A rapid turn-over may bring more beaucratic chaos than it does desirable change.

Public administration presents a somewhat different state of affairs, though again there are wide variations. The average tenure of bureau chiefs seems to be fairly constant. As we have noted, the average appointment and current ages were about the same for both 1926 and 1938. Because of this stability we are justified in doubling the average elapsed period of service in order to obtain a rough estimate of the average total term. Since the average elapsed period of service in 1938 was 5.6 years the total terms would run about 11 years. While this is not as long as the average terms of the top corporation executives, it may be considered satisfactory.

Above the bureau level, however, the holders of public office are much more volatile as to tenure. Thus, the average term for Secretaries, Under Secretaries, and Assistant Secretaries is only 3 to 5 years. The average period of service for our last eight Presidents and for all our Presidents combined has been about 5 years. Whatever the political merits of rapid turn-over, they are largely demerits when viewed from an administrative standpoint.

Walter Sharp saw in the transitoriness of the French Cabinet one of the prime causes of bureaucratic inefficiency in that nation's government.[15] We are more fortunate in the United States, for it is an unusual French Cabinet that lasts more than a year. However, we do not wholly escape the problem. Thus, in his blast against governmental bureaucracy in the United States, James Beck stated that "the heads of departments and their Assistant Secretaries hold office for comparatively short periods of time and they cannot during such short periods become familiar with all the duties of their departments—certainly not of the more technical phases of such duties. The consequence is that the heads of departments make nearly, if not all, of the decisions in name only, while the case is actually developed * * * [by] a subordinate in the department." [16] President Taft believed that the short terms of the top departmental officials had the result that "for a year and a half, at least, sometimes for a longer period, it throws the administration of the department into the complete control of minor subordinates." [17] These may be overstatements for purposes of emphasis but they indicate an actual problem. Of course, a somewhat similar difficulty exists when a new corporation president takes office, but his relatively longer term means that such periods of poor coordination need less frequently occur.

Thus, on the basis of turn-over of leadership, big business compares favorably with Government. Both business executives and bureau chiefs have quite satisfactory terms of office. Above the bureau level, however, turn-over is generally more rapid—too rapid, in fact, for effective administration.

Finally we should mention briefly the ability of the two groups to attract executive talent. Three elements may be mentioned: Salary, security, and prestige. Annual salaries of over a hundred thousand dollars for the top men are common among the largest corporations, though of course there are variations. Since most top executives have risen within their companies, however, and there is little cross-over among companies, the variations do not result in a flow of executive tal-

[15] Walter R. Sharp, French Civil Service: Bureaucracy in Transition (New York: Macmillan, 1931), p. 33.
[16] James M. Beck, Our Wonderland of Bureaucracy (New York: Macmillan, 1932), p. 173.
[17] Quoted in ibid., p. 121.

ent to those paying the highest salaries. Remuneration schedules appear to be at least sufficient to make the top positions attractive from that angle to subordinate executives within particular concerns—which is about all that matters in practice, except perhaps in the case of the railroads where there is some transfer among them.

Judging from the length of service of the top executives of the largest corporations, security of tenure at that level at least would also seem to be adequate. Likewise the position of head of one of the large corporations carries with it a good deal of prestige in the corporate family and is therefore an inviting goal.

In comparison with business, government is generally less attractive from the standpoints of salary and security for men at the top levels. In all of government there is no salary of a hundred thousand dollars. The term of office of those above the bureau level is also considerably shorter than that which obtains in the largest corporations. In regard to the element of prestige, however, the situation is different, for identification with the public service has always appealed to men and in recent years this attraction has considerably increased due in large part to the expanding role of government in modern life.

In summary, therefore, it may be said that business leadership often contributes to bureaucracy because of defects in regard to age, narrowness of outlook, and the too frequent resort to seniority in making promotions. The rate of turnover among the top business executives of the largest corporations is small—in fact, so small that complaints are sometimes made of stoppage at the top. In comparison with business, Government executives are no older, they probably have a broader outlook, and seniority has been less important in appointments above the bureau level, while tenure, at this point, on the other hand, has been relatively short. The prestige attached to the top governmental positions has been as great as that of the top business positions for the past decade and will probably continue to be high, though the attractiveness of salary and tenure are somewhat below the level of the major positions in big business. In short, the defects of leadership contributing to bureaucracy bulk about as large in business as they do in Government.

A low level of morale.—In addition to effective leadership, a prime requisite of a live, responsive, unbureaucratic enterprise is a high level of morale on the part of its employees. High morale is due to a number of factors, even a cursory examination of which would take us too far afield. Some of the more important, however, may be mentioned. These are adequate wages, reasonable hours, good working conditions, a degree of job security, some possibility of promotion, fair, nondiscriminatory treatment, and a psychological identification with the company or a part of it.

The adequacy of remuneration is difficult if not impossible to determine on an absolute scale. Many so-called necessities today were luxuries or entirely unknown yesterday. On a comparative basis, however, the position of the giant corporations may be stated. Thus, in general, the nation's largest companies pay wages and salaries and allow vacations, and the like on a somewhat more liberal plane than do the small companies in their respective industries. On the other hand, there is little general difference with regard to hours.[18]

[18] Our observations and the statements of the executives of large companies on these points are buttressed by a number of reports on specific industries which have been issued by the United States Bureau of Labor Statistics and by a summary report of these data in process of preparation by that Bureau for submission to the Temporary National Economic Committee.

Working conditions in the largest concerns appear as a rule to be above those found in the smaller companies. Likewise, job security seems more stable, though there are wide fluctuations among industries. Pension and other benefit plans are also more characteristic of the large companies, though the social security movement is strong testimony to the inadequacy of industry's care of its workers in their old age.

In the matter of discrimination, various classification systems—whereby equal pay for equal work is reasonably well guaranteed—are probably more widely used in the large than in the small corporation, though they have not been carried to any degree of refinement in either case. Allegedly unjust treatment growing out of interpersonal relationships is probably no more prevalent in one group than in the other, though individual concerns vary widely in the effectiveness of their personnel policies on this point.

As for the possibility of promotion, the large corporation offers a longer road but a larger reward at the end, while in the smaller concern an individual may get to the top more quickly because there are fewer intervening stages. However, it is widely recognized that substantial opportunity for promotion does not exist for a large proportion of the workers in either case. There simply would not be enough supervisory jobs to go around if all employees were capable of holding such positions. Most of them, therefore, must look forward to remaining more or less at their current levels despite the havoc this may visit upon the American tradition of "getting ahead." Nevertheless, many executives of the large corporations recognize the deficiencies of their means of uncovering talent soon enough to set such men on the road to advancement. Revised systems pointing toward this objective are being developed in a few of the big concerns; the smaller ones rely largely on personal, informal methods of identifying and promoting potential executives.

Finally, an active psychological identification with the company on the part of the employee is of great value in maintaining morale. A corporation executive has remarked, for example, that his company—

> has always had a loyal and enthusiastic organization. How is this done? In the first place, employees are very early indoctrinated. The new employee is given a pamphlet telling about the history of the company, its principles, and its heroes. Then, too, many of the employees are stockholders. This gives them a big interest. Finally, the company has been able to sell the corporate myth—it is honest; it takes care of its own; we are all one big family; we are the biggest and best in the field.

In like manner the slogan "The message must get through,"[1] together with its supporting examples where difficulties were surmounted, is a powerful symbol by which to keep up morale in a telephone company.

The large corporation, however, works under handicaps when it seeks to have all of its employees positively identified with it. So much that touches the employee is impersonal, and identification is largely a personal matter. The result is that much of the employee identification that exists is chiefly with small groups within the enterprise. T. N. Whitehead argues that—

> in spite of endless talk about the value of "esprit de corps," "morale," and the like, many executives become visibly uneasy when this sentiment begins to build up in the only way possible to it. What is asked of the worker is a vivid loyalty to some high abstraction variously referred to as "Company policy," "The firm," or even "The principles for which we stand.

> But loyalty is a social sentiment and it is built on routine collaboration, starting with quite small groups within the structure, and gradually spreading outward as these groups being to integrate among themselves. The progress of loyalty is from small to larger associations; this is the story of American federalization; it represents the historical growth of most large companies, and it is the story of integration in any wide association of human beings.[19]

This tendency of loyalties to small groups is no doubt partly responsible for the development of cliques of which so many executives complain. The problem of extending such narrow loyalties to broader spheres is a task of management which is far from solved in the big corporation.

Perhaps the best single, over-all indication of the level of morale in an enterprise is the rate of turnover among its employees. It is the replacement figure that is especially important here because in large part this represents either dissatisfaction with the company on the part of the employee or on the part of the employer with the worker. Separations or accessions alone may be too greatly influenced by changes in the condition of business to be a reliable indication of the level of morale.[20] Some seasonal industries, of course, show a high rate of separations and accessions over a period of a year, but this need not necessarily mean that morale is low. In fact, it may well be fairly high if wages are adequate on an annual basis and the workers are fairly sure of being rehired. Use of the replacement rate helps to uncover such conditions.[21]

Data are available from which a rough indication of the replacement rates in both small and large business may be obtained. The raw figures relate to whole industries and are confined to monthly changes. Changes with a cycle shorter than a month or for particular concerns are not shown. Such replacement rates for 20 large, separate industries and for 144 manufacturing industries combined are shown in tables XV and XVI.

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[19] T. N. Whitehead, "Leadership Within Industrial Organizations," Harvard Business Review, XIV Winter, 1936), p. 164. See also his Leadership in a Free Society (Cambridge, Mass.: Harvard University Press, 1936).

[20] It must be acknowledged, however, that in the declining phase of the cycle wholesale separations doubtless have a bad effect upon morale. Everyone wonders whether or not he is next.

[21] The replacement rate is the ratio of separations or accessions, whichever is the smaller, to average pay roll. This shows the extent to which men hired are taken on to replace men who have left t e company. During a period when men were being added but none were being laid off, the replac t rate would be zero. Using the accession rate as a turnover indication of morale would give an erroneous impression of morale.

TABLE XV.—*Replacement rates of personnel in 20 large industries, 1938* [1]

Month	Automobiles and bodies	Automobile parts	Boots and shoes	Brick, tile, and terra cotta	Cigars and cigarettes	Cotton manufacturing	Electrical machinery	Foundries and machine shops	Furniture	Hardware
January	2.34	4.82	2.25	6.79	5.15	3.92	1.32	1.53	6.43	1.78
February	2.38	5.84	1.82	6.10	1.53	3.93	1.04	1.49	5.06	.97
March	2.44	6.61	2.27	6.67	2.94	3.49	1.42	2.10	3.40	1.32
April	2.75	5.40	1.14	7.25	2.00	3.20	.96	1.69	3.52	.94
May	1.91	3.81	1.36	7.02	1.80	4.09	1.32	1.31	4.28	.90
June	2.54	4.65	4.05	5.48	2.49	4.27	1.82	1.80	3.67	1.19
July	3.92	4.31	2.00	5.06	2.19	4.34	2.00	2.29	2.89	2.34
August	10.36	4.32	2.16	4.63	1.84	3.10	1.94	2.81	2.56	1.99
September	3.54	2.96	1.82	3.78	2.95	3.80	1.76	3.05	2.59	1.62
October	1.79	2.72	1.57	3.17	2.69	3.39	1.50	2.90	3.29	1.61
November	2.46	3.03	2.23	4.92	2.29	2.60	1.52	3.59	4.40	1.22
December	2.51	4.88	3.12	3.43	1.85	3.43	2.89	2.24	3.09	1.76
Total for year	38.94	53.35	25.79	64.30	29.72	43.56	19.49	26.80	45.18	17.04

Month	Iron and steel	Knit goods	Men's clothing	Petroleum refining	Radios and phonographs	Rayon	Rubber tires	Sawmills	Slaughtering and meat packing	Woolen and worsted goods
January	1.15	2.75	3.26	2.05	5.41	7.62	1.19	6.72	6.38	7.99
February	1.46	3.09	3.84	.88	3.07	2.33	1.31	4.73	5.18	5.30
March	.92	3.76	4.33	1.83	2.57	2.46	1.37	6.02	5.69	3.93
April	.83	2.59	1.87	1.34	4.67	2.36	1.65	5.92	6.42	5.08
May	1.37	2.37	4.28	1.53	6.68	2.21	1.75	5.19	5.10	5.76
June	1.12	2.96	8.54	1.72	5.37	1.77	1.32	5.59	5.94	6.22
July	1.98	3.56	3.93	1.15	1.66	2.98	3.45	4.85	6.14	1.92
August	1.45	2.66	2.32	2.26	3.41	1.78	2.02	5.47	6.35	4.85
September	1.56	2.14	3.40	1.30	2.42	2.23	1.26	5.97	6.35	3.00
October	1.29	1.96	4.29	1.65	3.91	1.94	1.79	4.68	5.82	5.17
November	1.25	2.15	3.92	1.01	3.21	1.25	1.07	3.95	6.71	4.61
December	1.48	2.46	5.08	1.33	4.22	1.94	1.32	4.41	7.62	3.71
Total for year	15.86	32.45	49.06	17.55	46.60	30.87	19.50	63.50	73.70	57.54

[1] Based on data published in issues of the Monthly Labor Review, May 1938–March 1939. The replacement rate is derived as follows: Whichever is the smaller of the separations or accession rates for each month for each of the industries is used as the replacement rate for each month. The rate for the year is obtained by adding the 12 items for each industry. This rate is, of course, smaller than either the total accession rate or the total separation rate for the whole year because the effects of cyclical or seasonal fluctuations in the total size of the pay roll tend to be eliminated.

TABLE XVI.—*Replacement of industrial personnel for 1938* [1]

	Median [2]	Arithmetic mean [3]
10 large relatively concentrated industries [4]	27.76	32.48
10 large relatively unconcentrated industries [4]	45.89	44.60
20 industries combined	35.70	38.54
Replacement rate for 144 industries [5]	39.01	

[1] Based on data published in the Monthly Labor Review, May 1938–March 1939. The selected portions of these data for 20 industries are given in table XV.

[2] The median value here used is the average of the rates of the 2 central industries.

[3] The mean used here is the arithmetical average of the average rates for the industries. No adjustment is made for size of industry, though all employ more than 25,000 persons.

[4] An industry is classified as concentrated if the 4 largest enterprises of industries employing more than 100,000 persons produce over 25 percent of the total output or if the 4 largest enterprises in those industries employing 25,000 to 100,000 persons produce over 35 percent. By inference this gives us a rough measure of the size of the concerns involved and provides a basis for comparing turn-over ratio in large and small concerns.

The 10 industries classified as concentrated are automobiles and bodies, automobile parts, boots and shoes, cigars and cigarettes, electrical machinery, iron and steel, petroleum refining, rayon, rubber tires, and slaughtering and meat packing. The 10 unconcentrated industries are brick, tile, and terra cotta, cotton manufacturing, furniture, foundries and machine shops, hardware, knit goods, men's clothing, radios and phonographs, sawmills, and woolen and worsted goods. See chart 1, supra, facing p. 5.

[5] This is a very rough figure derived by taking the monthly total accession, or separation rate, whichever is the lesser in a given month, and totaling the 12 items. The total accession rate for the 144 industries was 46.20 percent of average pay roll, and the total separation rate was 49.20. The replacement rate is of course smaller because it tends to eliminate the effects of pay roll fluctuations of cycles longer than 1 month.

We have divided these large industries into 2 groups of 10 each; 1 includes in general the large and the other the relatively small concerns. The dividing line is, of course, dim and arbitrary. We have then assumed that the combined turn-over rates for the industries that are characterized by large concerns are typical for large companies. Likewise, the rates for those characterized by small concerns indicate the rates for small companies. We recognize that variations may be wide in individual cases but we believe that comparisons between the two groups are roughly valid.

On this basis the rate of replacements for small concerns appears to be about half again as large as the rate for large ones, the respective percentages being roughly 45 and 30. Thus, even without the effect of business cycles the average employee remains with the average company only about 3 years. He stays somewhat longer, however, in the large enterprise than he does in the small one. Rough as these figures are, we feel justified in basing upon them the conclusion that, judged by this criterion alone, the level of morale in large companies is at least as high as in small ones and that in all probability it is somewhat higher. Apparently the large companies have more than compensated for the handicap of impersonal size. This is of course relative to the level of morale attained by small concerns; it is clear that both groups have much room for improvement.

Before leaving for the moment this condensed examination of morale, a few brief comparisons should be made with government. In regard to the factors of nondiscriminatory treatment, good working conditions, reasonable hours, and adequate wages, government is equal to the level of the more advanced private enterprises and is considerably above the general average for employees up to the $2,000–$3,000 level. Beyond this, however, private employment pays progressively higher salaries.[22] Employee identification in government is probably also on as high a plane as that attained by private industry. Regarding the possibilities of promotion, however, there are some dis-

[22] Cf. U. S. Personal Classification Board, Closing Report of Wage and Personnel Survey (Washington; Government Printing Office, 1931), pp. 114–120, 243.

crepanies, for advancement is probably more regular and certain in the civil service, though it is limited enough in either case. In those places "where the lightning strikes," of course, advancement may be more rapid and more extended in the large corporation. On the score of security the civil servant has clearly the more advantageous position, though advances along this line are being made by many of the large corporations. Powerful incentives for effective work and high morale are not lacking in the public service, for patriotism and altruism, together with pride of craftsmanship and a good job well done operate with particular force in government.[23]

The effect of these factors on the replacement rate in government is indicated in tables XVII and XVIII. The rather large sample of Federal employees here examined doubtless has its inadequacies but it should be reasonably reliable in portraying the general situation.[24] The annual replacement rate is from 13 to 16 percent for the 2-year period ending June 30, 1938. In other words, barring general shifts in the size of the various agencies, the average employee remains in the service for a period of about 7 years. Obviously one cannot say that morale in the Federal service is therefore about twice as high as in the large corporations. The element of security is probably given too much weight in these turnover figures to permit their use as accurate and absolute indicators of morale. Moreover, morale itself can scarcely be measured in quantitative terms. We do believe, however, that the replacement rates indicate that it is at least as high in the Federal service as in the large corporations. Individual concerns, of course, may have a higher level, but we doubt that this is true for the group as a whole.

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[23] See Marshall E. Dimock, "The Potential Incentives of Public Employment," American Political Science Review, XXVII (August 1933), pp. 628–636.

[24] For one thing, no monthly break-down of the data is made, as was possible with the industrial data. However, the relative stability of Federal employment tends to make the resulting distortion quite small. Moreover, we are here able to examine separate agencies while the industrial data were for whole industries. Fortunately, the tendency of error appears to be in the same general direction for both groups, which increases the validity of comparisons.

TABLE XVII.—*Number and rate of appointments and separations in the Federal service for the fiscal years ending June 30, 1937, and June 30, 1938* [1]

Department or agency	Year ending June 30, 1938					Year ending June 30, 1937				
	Average number on pay roll	Appointments		Separations		Average number on pay roll	Appointments		Separations	
		Number	Percent	Number	Percent		Number	Percent	Number	Percent
Office of the President	45	3	6.67	29	64.44	44			5	11.36
State	5.264	597	11.34	313	5.95	4,790	277	5.57	221	4.45
Treasury	68,113	10,297	15.12	11,190	16.43	73,056	9,864	13.50	10,741	14.70
War	89,832	20,225	22.51	13,661	15.21	84,340	13,900	16.55	10,565	12.53
Justice [2]	10,283	1,213	11.80	805	7.83	10,124	327	3.23	265	2.62
Post Office [3]	1,725	162	9.39	100	5.80	1,695	109	6.43	81	4.78
Navy	67,993	9,449	13.90	14,807	21.78	71,156	2,342	3.29	6,459	9.08
Interior [4]	41,793	7,227	17.29	4,934	11.81	45,686	16,000	35.02	14,080	30.82
Agriculture	89.021	17,101	19.21	18,076	20.31	85,786	12,176	14.19	16,901	19.70
Commerce	16,214	9,226	56.90	6,683	41.22	15,553	5,639	36.03	9,394	60.01
Labor	9,728	1,740	17.89	1,778	18.28	15,379	1,046	6.80	1,056	6.87
Alley Dwelling Authority	15					12				
American Battle Monuments Commission	124	1	.81	6	4.84	56	1	1.79		
Board of Tax Appeals	125	1	.80	1	.80	131				
Central Statistical Board	40					58				
Civil Service Commission	1,094	199	18.19	109	9.96	1,188	54	4.55	181	15.24
Commodity Credit Corporation	94					111	3	2.70		
Coordinator for Industrial Cooperation [5]	5	1	20.00	4	80.00	39	20	51.28	47	120.51
Electric Home and Farm Authority	90	46	51.11	12	13.33	53	32	60.38	5	9.43
Employees' Compensation Commission	427	305	71.43	72	16.86	415	56	13.49	36	8.67
Export-Import Bank	12	2	16.66	4	33.33	13				
Farm Credit Administration	3,582	441	12.31	616	17.20	4,718	273	5.79	418	8.86
Federal Communications Commission	595	136	22.86	135	22.69	661	77	11.65	152	23.00
Federal Deposit Insurance Corporation	856	176	20.56	104	12.15	805	72	8.94	47	5.84
Federal Emergency Administration of Public Works	4,685	639	13.64	2,322	49.56	9,241	1,275	13.80	4,284	46.36
Federal Home Loan Bank Board	328	18	5.49	44	13.41	298				
Federal Housing Administration	3,172	1,883	59.36	834	26.29	3,590	806	22.45	1,053	29.33
Federal Power Commission	442	159	35.97	72	16.29	365	82	22.47	36	9.86
Federal Savings and Loan Insurance Corporation	40	34	85.00	15	37.50	18				
Federal Trade Commission	563	92	16.34	52	9.24	580	32	5.52	25	4.31
General Accounting Office	4,926	826	16.77	582	11.81	4,894	111	2.27	359	7.34
Government Printing Office	5,505	520	9.45	664	12.06	5,539	395	7.13	278	5.02
Home Owners' Loan Corporation	14,350	50	.35	296	2.06	15,575	6	.04	1	.01
Interstate Commerce Commission	2,345	480	20.47	186	7.93	2,183	294	13.47	122	5.59
Maritime Commission	1,118	288	25.76	132	11.81	771	106	13.75	43	5.58
National Advisory Committee for Aeronautics	491	55	11.20	40	8.15	442	103	23.30	62	14.03
National Capital P rk and Planning Commission	21	1	4.76	1	4.76	18	1	5.56	2	11.11

National Labor Relations Board	586	442	75.43	259	44.20	183	71	38.80	12	6.56
National Mediation Board	68	1	1.47	1	1.47	68				
Panama Canal	10,665	309	2.90	255	2.39	10,476	394	3.76	244	2.33
Paris International Exposition	13	1	7.69	4	30.77	6			4	66.67
Railroad Retirement Board	1,209	1,064	88.01	598	49.46	693	238	34.34	28	4.04
Reconstruction Finance Corporation	2,758	174	6.31	515	18.67	3,064	5	.16	443	14.46
Rural Electrification Administration	457	113	24.73	70	15.32	405	40	9.88	14	3.46
Securities and Exchange Commission	1,130	257	22.74	185	16.37	1,115	128	11.50	114	10.22
Smithsonian Institution	475	74	15.58	62	13.05	479	15	3.13	21	4.38
Social Security Board	8,572	3,967	46.28	900	10.50	3,599	2,676	74.35	443	12.31
Tariff Commission	303	26	8.58	21	6.93	304	18	5.92	14	4.61
Veterans' Administration	34,967	6,640	18.99	5,721	16.36	35,437	7,711	21.76	8,203	23.15
District of Columbia Government [6]	12,500	2,592	20.74	1,493	11.94	12,500	1,008	8.06	687	5.50
Architect of the Capitol [6]	500	54	10.80	34	6.80	500	42	8.40	39	7.80
Library of Congress [6]	1,000	188	18.80	118	11.80	1,000	166	16.60	119	11.90
Total	520,259	99,495	19.12	88,915	17.09	527,535	78,051	14.80	87,304	16.55
Transfers [7]		7,481		4,025			6,315		3,625	
Total less transfers	520,259	92,014	17.69	84,890	16.32	527,535	71,736	13.60	83,679	15.86

[1] Compiled by Statistical Division, U. S. Civil Service Commission. Refers only to Departments and Agencies from whom the Civil Service Commission rceives regular reports of changes in personnel. Some of these nave in the past failed to make prompt and complete reports of changes, as a result of which the figures in the table are probably not complete.

[2] Includes employees of the judicial branch of the Federal service.

[3] Includes only departmental employees in the Post Office Department.

[4] Includes the National Resources Committee.

[5] Abolished Oct. 1, 1937.

[6] Number of employees estimated.

[7] Discrepancy between appointments and separations by transfer is due to the failure of departments and agencies to indicate clearly on their reports the exact nature of action.

TABLE XVIII.—*Replacement rates of Federal service personnel* [1]

	Year ending June 30, 1938		Year ending June 30, 1937	
	Number	Percent of average pay roll	Number	Percent of average pay roll
Total average number on pay rolls of reporting agencies	520, 259	100. 00	527, 535	100. 00
Gross replacements [2]	88, 915	17. 09	78, 051	14. 80
Gross replacements less indicated transfers	84, 890	16. 32	71, 736	13. 60
Replacements adjusted by subtracting larger transfer number from gross replacements [3]	81, 434	15. 65	71, 736	13. 60
Total net replacements for individual agencies [4]	78, 997	15. 18	68, 996	13. 08

[1] Compiled from data in table XVII.
[2] Whichever is the lesser of total appointments or total separations.
[3] Since the reporting agencies indicated more accessions than separations by transfer for each year, the larger figure is used here to indicate actual transfers. The assumption is made that the discrepancies involved are caused by omissions in indicating that particular transfers have taken place.
[4] The total replacements indicated here are derived by ascertaining the replacements (whichever is the lesser of appointments or separations) which occurred in each reporting agency and totaling the items. Transfers are not subtracted because they refer to interagency movements and do not necessarily affect intra-agency turn-over.

Habit and inertia.—A third personnel cause of bureaucracy—in addition to the shortcomings of leadership and a low level of morale—is the influence of habit and inertia. Obviously the world could not go on without habit. If all decisions had to be remade every day the human race would become extinct. Habitual responses are particularly important in complex organizations such as large corporations. Only the broadest of decisions and directions can be made from the top. A high executive cannot be expected to know all the details in his enterprise, including those of the machinery whereby response to decisions or orders is obtained. He must know what strings to pull or what buttons to push in order to get the desired results. Beyond that he must depend largely upon the habitual responses of the organization which have been built up over a period of years.

Once a system of habits has been developed and put in motion, however, its inertia is tremendous. It is not easily diverted from its course. Speaking from his rather broad experience, the late James O. McKinsey has said:

> One of the dominant characteristics of human nature is the inertia to change. As a consequence, the majority has always resisted change, and even when changes become inevitable, it has sought to retard their accomplishment as much as possible. Consequently, changes in industrial operations and in economic methods have been effected very slowly during most of our industrial history. * * * Occasionally an executive has departed from the established custom and achieved success by being original; most of those who attempted to do this, however, have failed, and, consequently, most executives have come to believe it the wiser policy to follow the accepted routine.
>
> When a major economic upheaval has occurred executives trained in the habitual method of thinking have not been able to adjust themselves to the new order and a new generation of leaders has been developed.[25]

"There is no pain like the pain of a new idea" is another way of expressing the tenacity of habit and the comfort which it brings. When one adds to these qualities the fact that fixed ways of doing things result in vested interests among the performers, the importance of habit as a rigidifying influence becomes more apparent. Not only

[25] James O. McKinsey, Organization Problems Under Present Conditions, p. 6. A corporation executive has somewhat cynically observed, "You can't change the thinking of our executives. Logic won't do it, the depression didn't, labor won't. There's only one thing to do: let them die off or get rid of them." While we think that this official doubtless was exaggerating, nevertheless his experience and resultant attitude indicate the existence of a pressing problem.

do men resist change because they do not want to be mentally disturbed, but also because their skills may be less valuable under new methods. The much maligned Machiavelli pointed out centuries ago:

It ought to be remembered that there is nothing more difficult to take in hand, more perilous to conduct, or more uncertain in its success, than to take the lead in the introduction of a new order of things. Because the innovator has for his enemies all those who have done well under the old conditions, and lukewarm defenders in those who may do well under the new.[26]

The effect of habit is probably nowhere better illustrated than in the pricing and "merchandising" of railroad passenger traffic. Some western and southern railroads demonstrated several years ago that low rates, comfortable equipment, and rapid schedules were actually profitable because so much extra traffic was induced to use the service that the additional costs were more than met. Some of the railroads in the now prosperous and thickly populated northeastern region, on the other hand—those that "have done well under the old conditions" —are apparently unable to abandon the idea that lower rates necessarily means less net income. The experience of the roads which has proved otherwise remains unconvincing. Thus, a habit of thinking can be a formidable obstacle to progress.

Whatever the nature and causes of the reluctance to move or to think or to work on the part of individuals, it is not only universally present, but manifests itself in a highly unbalanced way. * * * Inertia is a factor of very much greater importance as respects things not attained but possible of attainment than it is as to things already attained but possible of loss. For example, people will exercise themselves tremendously, sometimes tragically, to retain what they have, yet will make almost no effort to secure very much larger benefits entirely within reach.[27]

Thus, habits, essential as they are, nevertheless clearly contribute to bureaucratic unresponsiveness.

Privitization of functions.—James O. McKinsey has aptly said:

It is a natural tendency for the head of each administrative unit to think primarily of the welfare of his unit. It is the problem of the major executive to provide for coordination of all these units so that confliction and lack of balance may not result to such a degree as to prevent the attainment of the major objectives of the business.[28]

Other executives agree that it is difficult to get men to look at their work from the standpoint of the enterprise as a whole. Perhaps it is too much to ask that a person take a broader view when he sees so many of his fellows vegetating in minor positions because they were not sufficiently aggressive in advancing their own interests. Executives complain that "A man's own record is all that counts," "A manager knows he will move on in 3 to 5 years. Therefore he wants to squeeze everything out in profits instead of planning a long-term program." Doubtless much of the reason for this view is the lack of proper incentives in the large corporations. As some point out, the balance sheet is often the only important criterion. This emphasis upon the financial record of particular subdivisions of an enterprise cannot help resulting in administrative sharecropping with its attendant wastes.

Self-interest and jealousy are potent forces, and unless they can be directed into channels which further the purpose of the enterprise as

[26] Nicolo Machiavelli, The Prince, translated by W. K. Marriott (New York: Dutton), p. 45.
[27] Chester I. Barnard, Collectivism and Individualism, pp. 11–12.
[28] James O. McKinsey, Organization Problems Under Present Conditions, p. 11.

a whole they may be very disruptive to it. The proper harnessing of these forces constitutes one of the prime and as yet inadequately solved problems of industrial administration. The forces themselves cannot be eradicated, nor is it necessarily desirable that they should be. As Friedrich and Cole have pointed out in a related circumstance—

As long as a "privitization" of functions can be prevented, the fierce enthusiasm of the functionary for his function, of the official for the power of his office, is desirable for the accomplishment of the ultimate purpose for which they exist. In this sense it may be said that a bureaucracy lusty for power is greatly to be preferred to a bureaucracy satisfied to grow fat on the livings which it has secured for itself.[29]

The desire for power.—Closely related to the jealousy and self-interest inherent in the privitization of functions is a desire for power. They have in common a desire for distinction. Chester Barnard believes that "the most dynamic of all characteristics of human beings from the social standpoint is the love of distinction." [30] Another corporation official goes so far as to say that—

Executives have large egos, and the success of a corporation depends upon giving them a chance to satisfy them. We must invent new incentives; the financial one shrinks, relatively, the higher up you go. Executives turn to new worlds to conquer.

In this same vein, in relation to control at the top, Berle and Means have suggested—

Just what motives are effective today * * * must be a matter of conjecture. But it is probable that more could be learned regarding them by studying the motives of an Alexander the Great, seeking new worlds to conquer, than by considering the motives of a petty tradesman of the days of Adam Smith.[31]

The desire for power and prestige is of such wide influence in the human breast that business leaders and their subordinates cannot be expected to be immune. The wish for more extended influence is particularly apparent in the "promoter" type of leader. He may win and lose several fortunes but he comes back, seeking to cross new horizons of influence. This urge is clearly present in the more common type of business leader who seeks steady if unspectacular expansion.

The extension of economic power today is generally carried on in apparently more refined ways than were common in the last century. The obstacle to increased influence may be as surely removed but the device of buying out is now more popular than the former "forcing to the wall." Naked methods are frowned upon, and the leader, in expressing his desire for influence and prestige, must fit into the pattern. Even though the roadbed is being made into an excellent highway, the attempt of the New York Central in the eighties to "free Pittsburgh from the thralldom of the Pennsylvania" by building another road might be considered rather expensive if tried today. Rather, a mutually satisfactory agreement would be reached—as was eventually done in this case.

A man's desire to expand his influence is of course not confined to intercompany relations; it is also expressed in intracompany matters. This is particularly apparent when a new type of office is created. The process has been repeated over and over in corporate history.

[29] Friedrich and Cole, op. cit., p. 86.
[30] Chester I. Barnard, Collectivism and Individualism, pp. 8–9.
[31] Berle and Means, op. cit., p. 350.

Thus, the general manager or executive vice president has become more than an assistant to the president. Likewise, when the office of comptroller was invented the comptroller became more than an accountant. In many companies he expanded his functions until he was almost the chief executive officer. In the readjustment which has since taken place he is still an influential executive but pressure from his colleagues has forced him to acknowledge that others may also be of importance in an enterprise. Of course, today there is wide variation in his functions. Sometimes the word "comptroller" signifies a man of real influence; sometimes it is little more than a title. At any rate, the history of this office illustrates the growth of power and its eventual limitation by the assertion of a stronger power on the part of competing executives. It is entirely possible that the personnel and public-relations officers of today will go through a similar cycle even though they may never reach the heights of importance once attained by some comptrollers.

Nor is the urge to increase one's importance limited to top executives; it extends throughout the hierarchy. A most common observation is the immediate attempt of a newly appointed foreman to seek unduly to assert his authority over his subordinates—to "show them who's boss." Related to such expression of command is the reluctance of some men, after they have been promoted, to relinquish activities with which they were formerly intimately concerned. Seemingly, increased authority does not detract from the appeal of the old realm of influence.

This continual struggle for influence and power cannot help affecting the corporate bureaucracy. Such desire on the part of the chief executive, for example, may lead the enterprise into unprofitable channels. Expressed internally, it often prevents an adequate decentralization and delegation of authority. The resultant bottlenecks of decision make the bureaucracy slow and inflexible, aggravating a tendency which inheres in all large enterprises. The struggle among executives creates friction and jealousy rather than cooperation,[32] and at the bottom the obnoxious expression of authority causes resentment and inefficiency in the ranks of the workers.

The desire to grow in importance cannot be eradicated even if it were desirable. In fact, it may well be the most effective of incentives. Thus, it has been said—

> The maintenance of incentives, particularly those relating to prestige, pride of association, and community satisfaction, calls for growth, enlargement, extension. It is, I think, the basic and, in a sense, the legitimate reason for bureaucratic aggrandizement in corporate, governmental, labor, university, and church organizations everywhere observed. To grow seems to offer opportunity for the realization of all kinds of active incentives—as may be observed by the repeated emphasis in all organizations upon size as an index of the existence of desirable incentices, or the alternate rationalization of other incentives when size is small or growth is discouraged. The overreaching which arises from this cause is the source of destruction of organizations otherwise successful.[33]

The problem—imperfectly solved as yet—is to keep the desire for increased scope of influence within its proper bounds.

Decline of the prod of competition.—It may be true that much of our progress is due to man's laziness, which urges him continually to discover easier ways of doing things or of obtaining what he wants.

[32] Some executives, however, maintain that the best way to define a job is to let the men work out the boundaries of their particular spheres for themselves.

[33] Chester I. Barnard, The Functions of the Executive, p. 159.

But the reverse is equally true: man's laziness creates a common tendency to let things slide when there is no effective prod or incentive to greater industry. Competition is one of the most important of these prods to activity, to progress through the threat to survival. Under the theory of atomistic competition it is an ever-present and ruthless force. Unless adjustment is made, a given business will speedily become extinct.

But the economic environment of the large corporation is quite different from this. We have already noted that a large sector of our economy is characterized by the relative absence of competition—certainly competition of the atomistic type.[34] As might be expected, of course, a relatively gentle or at least nonruthless type of rivalry affects the personnel of the corporate bureaucracy. But some executives maintain that the large corporations are so free from the acute stages of competition and have such immense reserves that their success is no real test of executive enterprise and capacity.

The depression, however, at least intensified competition for the consumer's dollar among quite different types of business. The resultant prod upon the bureaucracy was much the same as though ordinary competition existed. Theoretically, management should seek constantly to maximize profits, and should never be satisfied merely because they appear to be adequate. But the urgency of the depression revealed how far from the truth that assumption is, because it reckoned without human laziness. The biggest companies felt the pinch and responded with increased attention to economies. For example, one large concern remained profitable throughout the depression simply by cutting expenditures to follow the reduction in revenue: "When revenues drop you figure out some way to make expenses drop correspondingly." Or again, practices are reflected in such remarks of executives of large corporations as "[The company] has always been a profitable business and we haven't had to worry about management principles very much—but it's clear we'll have to increasingly." "As long as things are rosy they might as well be left alone." "Executives are content to muddle along as long as profits are satisfactory. Attention to operating matters is the child of adversity." "Now that the depression is past all interest in management has disappeared." "There is a point beyond which business organization becomes progressively inefficient and unresponsible. Probably it is because it becomes so powerful that it gets arrogant and careless. It knows it doesn't have to compete." "We wait until [our chief competitor] has tried out an idea and made it work. Then we do the same thing. We can afford to wait." Thus, the absence of the continual prod of competition becomes apparent when companies are large and have a comfortable portion of the market to themselves.

Decline in competition stems from yet another aspect of the large corporation. When business is small and competitive, the executive has a rough measure of his own efficiency in its financial success. When companies are combined into a large corporation, however, and their activities are consolidated into functional departments, the basis of comparison disappears. The efficiency of the production manager cannot be measured, for example, by the quantity of goods which the sales manager is able to dispose of. The result is that each

[34] Supra, ch. I.

department and its functional subdivisions becomes a unit insulated from the general impact of competition. With this pressure removed, the natural tendency is to slacken the pace.

It is easy to become oversentimental about competition but there is no doubt that its decline in respect to big business contributes to corporate bureaucracy. Of course, it is also true that the lack of competition in government or the church contributes to bureaucratic unresponsiveness in those realms as well. Human beings tend to act like human beings whatever the type of employment in which they may be engaged.

Summary.—Large corporations do not escape from the personnel causes of bureaucracy in its rigidifying, unresponsive aspects, any more than they do from its structural causes. Leadership is sometimes defective because of advanced age, lack of broad vision, or promotion on bases other than merit. Many companies fail to adopt policies designed to maintain a high level of morale on the part of their employees. Habit and inertia are potent bars to progress and change in the corporation as in other human relations. The tendency to privitize functions, to use office for personal rather than corporate advantage, is apparent here as elsewhere. The desire for increased influence is as plain at the lower levels of the corporate hierarchy as it is at the top. Finally, our limited examination has highlighted the effects of the decline of competition. With this prod removed, the pressure toward improvement is often relaxed.

It is not accurate, therefore, to think of corporations as things apart, as far as the obtrusion of bureaucracy is concerned. They are just as subject to forces tending toward bureaucracy as are other combinations for human endeavor.

PART III

MANAGERIAL CORRECTIVES OF BUREAUCRACY

CHAPTER VII

STRUCTURAL METHODS

The administrative antidotes to the evils of bureaucracy are as numerous as the structural and personnel causes which we have discussed. In fact, all administrative techniques may affect them. Thus, a complete survey of possible remedies would require a comprehensive treatise on corporate management and is obviously beyond the scope of this monograph. Nevertheless, we may briefly indicate some of the correctives which relate directly to the particular characteristics and causes which we have mentioned.

This chapter is a condensed summary of some of the successful practices relating to administrative structure which we have found corporations to be using, or which we think they should use, in order to combat the ill effects of bureaucracy. It is intended simply to indicate avenues of approach; it is not a manual of procedures which may be applied directly to given situations. Even if all corporations were alike, this would necessitate too long and detailed a discussion to be useful, while the actual heterogeneity of corporation problems makes such an attempt impracticable under any circumstances. The following discussion, therefore, relates to the general principles and methods which resourceful administrators may use in counteracting bureaucratic divisiveness, inflexibility, unresponsiveness, and waste.

The structural correctives to which this chapter is confined fall quite naturally into a number of groups. The first concerns the clear definition of objectives, responsibilities, and authority.

Definition of objectives, responsibilities, and authority.—A prime requisite of managerial unity is a clear understanding of objectives. "We don't know where we're going but we're on our way" is an attitude which should have no place in business enterprise. Of course, the future cannot be accurately foretold, but a working goal can and should be determined. It is perhaps true that "the greatest need of the average business is a more perfect recognition of its larger purpose." [1]

A carefully expressed, impersonal purpose for the enterprise as a whole may not be vital to the small concern, where loyalty to the wishes of the dominant executive may be adequate if they are sufficiently clear. In the large business, however, personal relationships are not so prevalent, and a substitute in the form of a corporate objective must be found in order to maintain morale and to direct the efforts of both executives and employees toward a common end. Only through such unity can the potentialities of the large corporation be even approximated. But a common objective contributes something more than this; it strikes some of the shackles of bureau-

[1] Webster Robinson, Fundamentals of Business Organization (New York: McGraw-Hill, 1925), p. 17.

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cratic inertia and releases human enthusiasm; it is a powerful spur to initiative and to sincere, loyal effort.[2]

A symbol or objective like "the best service at the least cost, consistent with financial safety" is broad and lacks something in definiteness. It is, however, more specific and may contribute more to morale and effort than the slogan "Maximize profits." As one executive pointed out, profits are only a byproduct of the realization of other objectives. Attractive service, minimum waste, efficient workers, and ample capital, as well as the ever important element of luck, all contribute to profits. The head of one large corporation has suggested, for example, that there are three main objectives of management: A return on investment sufficiently high to insure the offering of ample capital; wages and other attributes of advanced labor policies adequate to attract a sufficient supply of qualified workers; and quality of product at a price reasonable enough to attract and satisfy customers. He maintains that—

> The first responsibility of management is to think through the objectives and make them known to all parties. A concern should figure that it is in business for a long time and hence be temperate and consistent. These three objectives, plus inspiring leaders, are all a corporation needs for good morale and institutional vitality.

The more definite the objective the easier it is for all administrative personnel to appraise their activities in terms of what they wish to achieve. It is difficult, of course, to give specific expression to a long-range objective, though most corporations could do better if they tried. Short-term goals, on the other hand, can be made satisfactorily precise if the proper machinery is established.

An essential part of good budgetary procedure is the selection of objectives for the period to be covered, their expression in measurable terms, and the allocation of resources to those ends. Though usually described in monetary units, budgetary objectives are often improvements in service, expansion of facilities or markets, and the like. Measurement may also be in nonmonetary units, however, such as a decrease in the average number of seconds in which a telephone operator answers a signal on the switchboard, or fewer customer complaints. When such subobjectives are clearly determined and communicated to all concerned, it is easier to combat bureaucratic tendencies toward diffusion of effort.

Unity of effort likewise demands that the policies of an enterprise, whereby objectives are reached, shall be definite. This is particularly the province of the top executives and of the board, if it is active. Clear definition in method and policy as well as in objective may reveal elements that are unclear or inconsistent. Improvement is thereby the easier because they can be corrected or eliminated.

Definition of responsiblities and authority also helps to overcome bureaucratic confusion and divisiveness. The determination of responsibilities is, indeed, a part of the process of clarifying objectives and policies. Essentiallly it is the assignment of portions of the objectives to specific executives and their subordinates. It defines a particular job and thereby facilitates its execution. The delimitation of spheres of authority also determines who shall give orders to whom, helps to eliminate the confusion caused by conflicting orders from several persons, and shows up instances of inadequate supervision.

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[2] Cf. Ordway Tead, "Purpose as a Psychological Factor in Management," Bulletin of the Taylor Society, X (December 1925), p. 254.

It is possible, of course, that if the definition of responsibilities and authority fails to allow for changes in these spheres, a rigidification may set in; this corrective of the evils of bureaucracy might then be more than counterbalanced by resulting inflexibility. There is, therefore, something to be said for the contention of some executives that it is best for the top men to work out their own spheres of influence. At least this method allows for change, even though confusion and bickering may also follow. We are of the opinion, however, that clear definition by one means or another is predominately advantageous and that inflexibility may to a considerable extent be offset by other means of adjustment. In the modern large corporation we do not feel that such definition has gone far enough.

Preventive maintenance applied to administration.—One promising method of supplying flexibility to an enterprise is what may be called preventive maintenance; that is, the periodic reexamination of existing policies, responsibilities, and even objectives, as well as of the more detailed practices which are accessory to them. Such a reexamination is particularly rewarding where important elements of administration have been clearly defined. Paradoxically, it is in this way that the possible inflexibilities resulting from clear definition may be discovered and eliminated.

We in America have paid much attention to economy and efficiency in the use of materials, but have often neglected improvements in the use of human resources. The idea of preventive maintenance is a good illustration of this. A number of companies, for example, have adopted the practice of periodically examining their equipment in order to repair or replace defective parts before they actually break down. To wait for a wrecked train to reveal a cracked rail, a series of rotten ties, or a weakened culvert is clearly poor economy. To wait for a boiler explosion to indicate that tubes have been burned out falls into the same category. On a lesser scale, the total cost of periodically examining telephone equipment may be less than that of making special trouble trips and of losing business and goodwill through defective service. At least the American Telephone & Telegraph Co. feels that preventive maintenance is a good investment.

As was pointed out in the preceding chapter, however, so continuing an interest in administration is not typical of the large corporation. Time studies of the activities of workers may be common enough, but a similar attention to administration is too often neglected except in periods of stress. So long as profits are adequate the executive finds it easier to check on his subordinates than on himself. When revenues drop or an aggressive competitor enters the field, on the other hand, he is apt to reexamine methods and objectives. This inconsistency is human but it has results which are bureaucratic. The stimulation of searching and continuing self-criticism is one of the greatest needs of corporate management. All too rare is the executive who maintains that because something has been done a certain way for 25 years it must therefore be the wrong way now. Even though his idea of the right method may leave something to be desired, he will prevent stagnation and retrogression.

We submit, therefore, that as an antidote to bureaucratic inflexibility and maladjustment to changing conditions, a procedure of periodic reexamination of corporation policies, objectives, and practices be adopted. These, of course, must be clearly determined. Such

a reexamination will probably require the full-time effort of a number of staff men, as well as much of the attention of the executives, who in addition must have the will to adopt changes when they appear advisable.

The duties of the staff men should include the constant checking of the results of policies, the examination and development of new practices, keeping abreast of changing social and technological conditions, and periodic recommendations to their superiors regarding the retention, abandonment, or revision of objectives and procedures. The executives, who are policy determiners, must so arrange their work as to have time for the continuing critical examination of these matters. Too often the modern corporation official is so immersed in day-to-day operations that he has no opportunity to consider the less pressing, though more important, questions of policy.

Placing this reexamination of objectives, policies, and practices upon a regularly recurring instead of a crisis basis would aid materially in meeting difficulties before they arise and in many cases would prevent their arising at all. As an antidote to bureaucracy it would keep administrative organizations from becoming over rigid, unresponsive, and maladjusted to a changing environment. Moreover, corporative self-criticism and the resulting corrective action is more effective and less disruptive than the same treatment administered by outside forces or agencies.

Standard practices and their proper place.—A third administrative antidote for the undesirable aspects of bureaucracy is the judicious use of standard practices. Rules of action are, of course, indispensable in the operation of any large enterprise. In no other way can the ideas of the best brains at the top be transferred into appropriate and unified action throughout the enterprise. Size makes personal direction impracticable in the modern corporate giant. The only workable substitute is the utilization of standard rules and procedures.

There is much that could be done to improve and enlarge the use of standard practices. In only a few of the large corporations are these clearly determined and handily published for the use of all affected portions of the hierarchy. Companies which are deficient along this line should remedy the fault. This means that certain staff employees devote themselves to the study of job requirements and the development of practices to meet them. Such work requires the time and expense that goes with continuous planning, research, and testing; but the companies that have given the process a thorough trial are usually convinced that it is money and effort well spent. Proper planning is a major deficiency of large corporations, though it must be said that as a rule they give it more attention than do the smaller concerns.

Even the best rules have a disconcerting way of becoming obsolete or inappropriate in exceptional, concrete situations. Only by constant readjustment to changing conditions can this be prevented. Periodic reexamination and revision of rules is one means to this end. In addition, a flexible attitude toward rules is required when the bureaucratic snare of legalism fastens itself upon the company. Few, if any, of the large corporations have entirely escaped from this species of red tape. Thus, it is risky for an employee to violate a regulation. So long as he obeys he has a covering excuse if his action is inappropriate. If, however, he exercises his own judgment contrary to a rule

he runs the risk of reprimand or discharge, even though the results of his action may not be particularly calamitous. Speaking of his company, an executive has remarked, "A man may be fired for one not very serious mistake."

The emphasis upon legality, which we noted in the preceding chapter as a prominent cause of the evils of bureaucracy, must be balanced against an emphasis on results. In order to reduce confusion to a minimum, weight must be given to obeying rules as such, but it is all too easy to overdo it. The only reason for rules in the first place is to obtain results. The end product is what really counts.

An interesting illustration of encouraging disobedience in order to obtain a desired end is found in political history. Empress Maria Theresa, of Austria, had a healthy skepticism regarding the acumen of her military commanders. Because of this she established the highest military decoration of the Empire to be bestowed upon officers who acted successfully in disobedience to their commanders. The penalty for failure, of course, was death. Perhaps military men become accustomed to such risks, for the decoration has been bestowed upon some intrepid officers. The late Emil Fey, for example, was honored with the Order of Maria Theresa for a maneuver which he carried out during the first World War. Although his superiors ordered him to retreat, he saw an opportunity for a successful advance and carried it out.

It would be a healthy thing if something of this attitude were encouraged in business administration. It might well assist in counteracting the tendencies to follow rules blindly and "to pass the buck" when there has been mistaken action. Initiative all along the line should be encouraged. Otherwise interest is lost, good rules turn into bad ones, and bureaucratic legalism with its attendant ossification settles upon the enterprise.

It is interesting that some corporations allow for disobedience to rules. In these concerns, when an executive adopts a different practice than that determined by the central office he is often allowed to use his own discretion. He is expected, however, to support his noncompliance with adequate reasons and to demonstrate the validity of his convictions with results. His reward is turning in a better operating record than his past one or those of corresponding officers in other parts of the company. We know of no case where honorary citation or other special recognition is given for intelligent disobedience.

In summary, it may be said that in order to check the tendency toward bureaucratic legalism, several related policies should be adopted by corporate management. Thus (1) standard practices and rules should be developed carefully, based on substantial factual material and continually reexamined for possible change, (2) care should be taken that too many rules are not promulgated "it is better to err on the side of too little standardization than to discourage initiative"; (3) except where uniformity is particularly important, discretion should be allowed to executives in applying rules, although it should diminish, of course, with the decrease in hierarchical rank; (4) emphasis should be on results rather than legality, and intelligent disobedience might even be rewarded. Moreover, the results to be emphasized should be more than a financial profit. Performance must be measured in other terms as well. An indication of some of these is discussed in the next section

Improvement of devices of internal coordination and control.—The evils of bureaucracy may be attacked through still a fourth group of practices, centering around the procedural attainment of unity and effectiveness. Broadly conceived, coordination and control may be considered as including practically all of management. Our discussion of them, therefore, will be limited to some of the highest of the high spots. Essentially, they are the processes of inducing persons to direct their efforts efficiently toward a common goal and of checking to see that these efforts are in fact efficient. They involve communication, inspiration, and some element of coercion, with communication probably the most important as well as one of the most difficult to attain in a large enterprise.

Our brief discussion will center around three main questions: What shall be communicated? What channels shall be employed? What use shall be made of the information? In terms of the causes of bureaucracy which we have discussed, coordination and control may be utilized as an antidote for divisiveness and separatism in the organization, for preventing the privitization of functions, for directing the desire for power into channels beneficial to the enterprise, and for compensating for the absence of competition.

Communication is of course a two-way process whereby the various parts of the enterprise learn what others are doing and thinking. The subject matter is as wide as the interests of the corporation itself. Policies and decisions must be communicated to all who are to carry them out. Executive action must be communicated to all affected parts of the enterprise, and especially to the top if operations are to mesh properly in a common endeavor. And when results come in, they too must be communicated to all sections of the company: the top executives must know them in order to determine whether or not to change particular policies, or to move, remove, or promote particular executives; the directors and the stockholders wish to judge the stewardship of the executives; and the rank and file employees need to appraise their own effectiveness.

To a considerable extent the usefulness of communicated results depends upon the units of measurement which are used. Profits and unit costs expressed in monetary terms are the most common. Although the cost-accounting systems of the large corporations could doubtless be materially improved, they are generally of a more advanced type than those, if any, used by the smaller companies. Despite their scientific, objective appearance, financial criteria inevitably have an element of arbitrariness. For example, any allocation of joint costs between several products or departments of an enterprise is arbitrary and at best an intelligent guess. However, our chief criticism of the measurement of results in the large corporation is the exaggerated reliance placed on the monetary aspects of profits and costs.

The monetary measurement of results is subject to severe limitations. For one thing, profits are often due to fortuitous circumstances quite beyond the control of management. A change in the price level, for example, may cause large losses or gains on inventory which will be reflected in apparent profits or losses. Overemphasis of profits and low costs may also lead executives to attempt to squeeze out everything possible in earnings and to ignore the resultant long-range effects on the enterprise. Administrative sharecropping can be as

destructive of the resources of a company as its agricultural counterpart often is of land. In the third place, financial standards are inappropriate, or inadequate, to measure most administrative activity. A reduction in the costs of running the personnel department, for example, may merely mean that a poor job is being done. A high record of collections may be obtained at the expense of losing many customers through harsh treatment. Low costs may be gained temporarily at the expense of driving employees unduly or by failing to promote men whose capabilities indicate that they should be advanced. A good financial record for part of an enterprise may mean a poor record for the company as a whole.

Some companies have made commendable progress in developing nonfinancial units by which to measure operating results. They start with some objective such as a yearly decrease in errors in handling customers' orders or even the development of new executive talent. The unit of measurement then is related to the particular objective. Errors per thousand orders are recorded as well as the subordinates of particular executives who are developed into executives themselves. In both instances the unit of measurement is related to major objectives of the corporation, objectives of a nonfinancial character which, however, influence the financial record.

Of course, financial measurements cannot be neglected. An enterprise must make expenses or be forced into bankruptcy. What is needed, therefore, is a system of appraising results in nonfinancial terms that will supplement an appraisal in financial terms. Thus it may be possible to overcome the shortcomings and distortions of the latter type used alone.

The how of communication is as important as the what. Superb information is of no value unless it is effectively made known to those who can use it. The simplest type of transmittal, of course, is face-to-face conversation. In many respects it is the best. The large concern, however, is constitutionally unable to make widespread use of this method. There are simply too many people involved for face-to-face contact throughout the enterprise. Nevertheless, it can be used within certain limits even in the giant corporation. Informal contact between executives is essential to a common viewpoint. As one executive pointed out, "When top executives begin to write letters, you know relations are strained."

Coordination through face-to-face contacts can be promoted in several ways. One of the simplest and most effective is to locate the various executives whose work is to be coordinated in the same building, preferably on the same floor. Under that arrangement, officials may and usually do quite easily compose their differences and mutually readjust their programs among themselves. It is surprising how physical distance augments mental distance, and correspondingly, how helpful to coordination a decrease in physical distance may be. The successful experiences of some corporations along this line should be copied whenever possible in others.

Interdepartmental committees also assist in meshing the various activities of an enterprise. The coming together of executives in such groups facilitates mutual adjustment. A formal committee with regular meetings is particularly useful in inculcating the habit of working together. Once this is established, the periodic meetings may be changed to occasional gatherings to deal with particular

problems as they arise, or the formal group may even be disbanded without weakening the habit of face-to-face contact when necessary.

As a safeguard, however, the various interested executives may be expected, or informally required, to get together themselves when the appropriate occasions arise. Some of the subsidiary companies of the American Telephone & Telegraph Co., for example, rely upon such informal methods for much of their coordination. If the traffic manager feels that his service record is not so good as it should be, due perhaps to imperfections in some phase of plant maintenance, he will consult with the plant manager and the two will generally reach an agreement. If another functional officer is also involved, the traffic manager will consult with him as well. Similarly an executive may call in particular subordinates as the need arises instead of holding regularly scheduled staff meetings when there is not enough interdepartmental business of interest to all. Informal, spontaneous coordination of this type, however, is dependent upon a well-ingrained habit of cooperation. In the absence of this habit it must be developed even if more formal means are necessary to accomplish it.

Much of the informal meeting of minds which we have been discussing takes place across, rather than along, hierarchical lines. The pattern of authority set by a particular hierarchy is commonly unable of itself to achieve the necessary degree of coordination. If jurisdictions are allocated on the basis of function, for example, a supplementary system of coordination covering particular territories or commodities should be established. It has usually been found, where tried, that this should be relatively informal in order to avoid confusion. "No man can serve two masters" has commercial as well as religious meaning. Short paths of communication are essential in overcoming the lethargy inherent in large size. Hierarchical channels are too long for emergency action and become congested if all matters for decision must follow them to the end. Informal horizontal communication, therefore, is of real assistance in overcoming the inflexibilities of corporate bureaucracies. There is much room for this type of improvement in the large corporations, and the resulting benefits of increased coordination and vital humanness are too great to be neglected.

To a certain extent, of course, formal methods are essential to the effective operation of the large enterprise. Policies and decisions which have widespread or long-term application must be carefully committed to paper. Enough distortion of meaning takes place under any circumstances, and if word of mouth is relied upon to carry the message through a number of steps it may be quite wide at the end of the process. Likewise human fallibility of memory changes the meaning of any decision over a period of time. Reducing policies to writing, therefore, not only clarifies them but also gives them a form which is capable of fairly accurate transmission and extended life. Nevertheless, it is a tool to be cautiously applied lest it degenerate into a mass of paper which will stall or at least hinder the administrative process.

Written reports of various kinds are universally employed both in business and in government to discover what is happening in the different sections of the enterprise and to provide bases for modifying undesirable action or results. Thus, most of the large corporations make extensive use of reports relating to items on the balance sheet

and profit-and-loss statement. It is probably true that financial statements are the most useful means of controlling business activity. A corporation must make ends meet or suffer extinction, and the effects of poor administrative methods are often revealed in high costs or low revenues. It is natural, therefore, to find the typical attitude among executives expressed thus: "The balance sheet is the best way we have of checking our men."

Some executives, however, recognize the inadequacies of balance-sheet reports as all-sufficient managerial control devices and have supplemented them with other means. Thus, the record of actual results compared with budget estimates or assigned quotas is widely used. The items may be much the same as those on the balance sheet, but the bases of comparison constitute a refinement beyond simple profit, loss, or expense. Some companies, noticeably the American Telephone & Telegraph Co., issue reports on matters not included in the balance sheet and the budget, such as, for example, the percentage of telephone-installation appointments which were kept and the reasons for missing those which were not. The graphic method of presentation is commonly used in order to show more clearly the broad outline of results. These performance items cover a wide range of subjects and constitute a significant group of data supplementary to the financial results. Much could be done to their advantage along this line by other large corporations.

Some corporations have established a sort of departmental channel of communication and control relatively separate from the rest of the hierarchy. The controller, or one who exercises similar functions in the keeping and examining of accounts and passing on expenditures, is sometimes so placed that he reports directly to the board or the finance committee. His men may provide budgetary estimates as well as audit accounts. The relationship, of course, has drawbacks as well as advantages, for the independent check which it provides may well be counterbalanced by the confusion which sometimes results. Thus, the head of one company with this system is supposed to have said, "It took me 6 years as president to discover that I wasn't supposed to control the controllers." The dual control is a source of friction. A thoroughgoing audit conducted by agents of the top men of the corporation would probably accomplish most of the benefits of this independent relationship without as much trouble. Nevertheless, the practice does emphasize the desirability of separate channels of information. Thus, for example, when these are the same as the channels of control, data may be slightly distorted lest it be used to the disadvantage of the members of the hierarchy through whom it passes. Separate lines obviate this difficulty.

The channels of communication for purposes of coordination and control are thus numerous and varied in large enterprises. Personal contacts, although useful, are necessarily limited by the size of the corporate giants Written reports are the mainstay of control, but relatively too much emphasis is placed upon balance-sheet items and too little upon other measurements of managerial efficiency. The independent controller has the advantage of freedom and the disadvantage of injecting administrative confusion into the bureaucracy; the chief benefits of the system could be gained in another way with less confusion. But just as results rather than legality are more important in relation to standard practices, so the use of the types of

information and of the channels of communication which we have been discussing is more important than the structure itself. Good information and transmission channels are of no value unless properly utilized.

Information has four principal uses in corporate management. First, it serves as the basis for policies and decisions. In these respects it is closely identified with objectives, or the direction toward which corporate activities are pointed.

Second, in relation to coordination and control, information is essential in harmonizing the activities of the enterprise, in correcting discrepancies and in providing incentives for greater productivity. To a considerable extent, harmonization of activities follows directly from the dissemination of accurate and sufficiently comprehensive information, for executives are then better able to see their roles in the corporate whole and to readjust their actions accordingly. In many ways this is a superior type of coordination because it depends on good will and a natural readiness to work together without the immediate threat of coercion. Of itself, however, the mere dissemination of information is usually not enough. Other uses of it must be made in order to limit the temptations of noncooperation or worse.

The third use of information is to check the legality or wisdom of executive action. In financial matters this is ordinarily done by means of the audit, which in the large corporation is typically a mixture of preaudit and postaudit or a check on legality and accuracy, and to some extent on wisdom, both before and after expenditures are made. The postaudit is usually more detailed and painstaking than the preaudit, which is brief, so as not to delay unduly administrative action. Executives may be given authority, for example, to make expenditures within certain specified limits on their own initiative and discretion. Expenditures in excess of these amounts may then be subjected to a type of preaudit, or specific authorization. Within the limits, however, funds are dispensed at the work of the particular executive, and much time and red tape are thereby saved. Ordinarily, the privilege is not abused because executives are reluctant to make illegal or careless expenditures which may later be embarrassing to them. Thus, since administration is a continuing process, the postaudit is effective without being obstructive.

The fourth use of information is to appraise the effectiveness of the various parts of the enterprise. This may be done by comparing the performance of a particular section with past performance, with budget estimates and with the records of corresponding parts of the organization. The basis of comparison provided by competition among large corporations through their relative profitability is markedly limited. Internal comparisons such as we have mentioned, therefore, substitute to some extent for the spur of competition and its ruthless weeding out of inefficient concerns.

Thus, comparison with past performance is one method of stimulating efficiency. "Each year you have to be a little better than the year before or there will be someone else in your job," expresses what appears to be the policy in some of the large corporations. The validity of such comparisons is obviously subject to the limitations imposed by changes in the conditions under which business is conducted. For example, earnings in a period of general depression can scarcely be expected to equal those of a prosperous year. Such com-

parisons do have the advantage, however, of dealing with the same unit of administration. Hence, differences which may invalidate a comparison between areas may not affect one of different time periods for a particular enterprise or part of an enterprise.

A comparison of results with budget estimates shows to what extent particular executives know and control their departments. It indicates where they have exceeded expenditures or otherwise disrupted the over-all plan of the company, and how far they have indulged in wishful thinking in making their plans. Only if results can be made to approximate estimates can the tool of the budget be useful as a planning and control device.

A comparison of the results of corresponding subdivisions of a company offers a parallel to and a substitute for competition among enterprises. Indeed, in some respects it is superior as an indicator of the relative effectiveness of particular executives. The organizational pattern of the enterprise, of course, must be suited to this type of control. The volume of sales, for example, cannot be compared with some aspect of the accounting department and thus provide a basis for judging whether the sales manager is a more effective executive than the chief accountant. The technique can only be applied to corresponding departments and subdivisions. Ordinarily this means territorial as well as functional divisions in the organizational scheme. Since the large corporation with its widespread activities usually has such a territorial pattern, it is especially adapted to control by comparison. Financial criteria are usually applied, though these are supplemented in some concerns by financial measurements of proficiency. The process could probably be usefully extended as an aid in combating the lethargy which often exists where competition among companies is absent.

Some reward should be provided for those men who, due entirely to their own efforts, compare favorably with others in the enterprise. Incentives should be closely allied with results. But it is equally important that results emphasize company welfare as well as personal advancement. Thus, an executive should not be given credit for an individual record gained at the expense of the company as a whole. Rather, he should be commended, for example, for developing subordinates into executive material even though through their promotion he loses that part of his staff which enables him to make a good showing. The delicate balance between individual and company welfare can be approximated only by introducing elements of both into the coordination and control system.

Thus, a thoughtfully conceived system of coordination and control will help to overcome several of the bureaucratic handicaps of big business. It minimizes the diffusion of authority and separatism; retards the use of executive office for private ends at the expense of the corporation; directs the desire for increased personal influence toward the common good; and compensates for the loss in drive resulting from a drop in competition. By emphasizing nonfinancial as well as financial units of measurement, furthermore, a proper control system within a large corporation may be even more effective than control through the imperfect pressures of the market under competitive conditions.

The coordination and control systems of some of the large corporations are generally poorly developed. Some of them may even

be called primitive in many respects. Very few companies have evolved as effective a system as they might. Many of the undesirable aspects of bureaucracy, therefore, which we find in the large corporations could be removed by simple improvements in coordination and control.

Decentralization.—Bureaucratic inflexibility may also be neutralized by intelligent administrative decentralization. This may be achieved in two important ways: first, by the scattered physical location of units of the enterprise, and second, by the delegation of discretionary power to subordinates. So far as physical decentralization is concerned, the large corporation is usually forced by its very size to adopt it. Its merchandising units, for example, must be accessible to its customers, and transportation and communication costs require that plants be located near the necessary materials and services.

As regards decentralization of authority, on the other hand, four basic factors are listed by L. Urwick. These are space, time, span of control, and morale.[3] When plants and staffs are scattered, for example, it is difficult for one person to supervise them. Delegation of authority, therefore, to those on the scene who need to deal with problems as they arise, helps to solve the difficulty. The influence of the time factor is somewhat similar. In general—

> Whenever a unit in an organization is situated where almost immediate reference to a superior authority is impossible some individual in that unit must be assigned responsibility for its general conduct and the corresponding formal authority. For this there are two main reasons: (*a*) In the event of emergency someone must take charge, and at once. If no single individual is responsible there is a risk of uncertainty and delay when they prove most disastrous. * * * (*b*) If the unit includes individuals whose work is interdependent, there should be someone on the spot whose duty is to forestall and to alleviate any differences which may occur between them. Coordination is a continuous task; it cannot be performed satisfactorily if the presence of the coordinator is intermittent.[4]

Important as are the impersonal factors of space and time, however, the psychological aspects are equally significant. Although it is not possible to indicate with mathematical precision the number of immediate subordinates that one man can profitably supervise, it is nevertheless clear that there are limits to an executive's effective span of control.[5] When an enterprise or a branch of it becomes so large that one person can no longer directly oversee its staff, it is essential that he either delegate authority or sacrifice efficiency and unity of action. The so-called exception principle of management stems largely from the necessity of reducing the scope of an executive's attention. Following this principle, subordinates attend to ordinary and recurring matters while their superior deals only with exceptional situations. That this procedure has thousands of years of tradition behind it is well illustrated by the favorite quotation of Mooney and Reiley:

> And Moses chose able men out of all Israel, and made them heads over the people, rulers of thousands, rulers of hundreds, rulers of fifties, and rulers of tens. And they judged the people at all seasons: the hard causes they brought unto Moses, but every small matter they judged themselves.[6]

Proper delegation of authority is also essential to morale. Executives sometimes emphasize that it is better for a man to make a few mistakes while exercising his own initiative than to allow no such

[3] See his "Executive Decentralization With Functional Coordination," Public Administration, XIII (1935), pp. 344–358.
[4] Ibid.
[5] See Marshall E. Dimock, "The Span of Control in the Federal Government."
[6] Exodus XVIII: 25, 26.

latitude. Initiative is one of the most important qualities of leadership, and "nothing is more destructive of initiative than interference from above which appears unreasonable, or authority inadequate to the task assigned.[7]

The executives of some corporations recognize the value of decentralization. The head of one large company, for example, insisted that local managers should be given fair measure of independence: "I have fought with my board and with my vice presidents," was his comment; "I contend that the local managers should be permitted to make mistakes. They're bound to make mistakes sometimes. Let them do it. What we're interested in are results." Another maintained that his company "would fail if it didn't decentralize. It couldn't be run from headquarters even if all its executives were supermen—as they are not." Nevertheless, the large corporations are faced with a difficult dilemma. They must allow decentralization for the reasons we have mentioned; but they must also insure over-all coordination, especially of policy, and clear emphasis upon the welfare of the company as a whole.

Striking the proper balance between centralization and decentralization is one of the most important problems with which management has to deal. Wherever it is successfully solved there would seem to be few other serious obstacles to the administration of any large enterprise. It must be admitted, however, that a complete solution is rarely attained. On the one hand, the executives at each level must have sufficient authority to handle situations as they arise. But on the other, broad policies, a system of control (particularly of the post-audit variety), the provision of advice, and programs for maintaining unity must be centralized. Just what degree of decentralization should be allowed in particular cases must depend upon the judgment of the officials involved and, all things considered, it is a remarkably difficult decision to make.

The necessity for a balance between the two extremes has been well expressed by James O. McKinsey:

> Most men pride themselves on being individualists, but no man can be in any true sense an individualist in our modern form of organization. He is only a specialized unit in a large cooperative enterprise. Most men work best, however, when they feel they are working as individuals, so the successful executive must strive to give the specialists he supervises such freedom that their initiative will not be restricted unduly, but at the same time, the executive must exercise such control as to provide sufficient coordination to prevent wasted effort and ill effects from the conflicting activities of these specialists.[8]

Perhaps a good executive viewpoint is that "centralization of author ity should always be regarded as a necessary evil to be kept to th minimum. It's a passport to bureaucracy in the present and, lik bureaucracy, it sterilizes the hopes of the future."[9]

An emphasis upon public relations.—A few companies find that administrative flexibility is aided by an emphasis on public relations, that is, giving primary consideration to the effect upon customer satisfaction of every act, even if it requires exceptions to general rules. This emphasis has three principal effects. First, public relations of the inward searching type requires a sufficient delegation of discretion to allow employees to handle specific cases according to the

[7] L. Urwick, op. cit.
[8] James O. McKinsey, Organization Problems Under Present Conditions, p. 10.
[9] L. Urwick, op. cit., p. 349.

circumstances involved. Serious illness, for example, may extend an otherwise shorter credit period; collection routine must be adapted to the necessities of the situation.

In the second place, emphasis upon public relations may change the standard practice used or even the organizational structure itself. In the Bell System, for instance, a customer with a complaint used to be shunted from section to section until he found the person who dealt with his particular trouble. The process was often long and disconcerting, and was finally changed as an aid to better public relations. Clerks were trained to handle a number of kinds of complaints or to know clearly to whom such matters should be referred. Now the customer sees only one person who handles the matter almost regardless of its nature. The customer is better satisfied and the employees have received a lesson in the importance of a pleased public. The same general idea carried further up the hierarchy may make it advisable to place general managers or even separate subsidiary corporations in charge of the activities of a particular area of a widespread company.

Finally, emphasis upon public relations is a touchstone to apply to alternative decisions in order to pick the best. Thus, the head of one large corporation has told a number of his executives: "I find it a useful device to ask myself the question, 'What would we do if we were faced with competition?' The answer often makes it very clear what decision should be made." Employees should be taught to apply the test of the possible effect of their work upon public relations. A number of executives testify that this serves as a positive deterrent to the ills of bureaucracy, for it keeps men alert and injects flexibility into rules that would otherwise be rigid.

A sixth managerial corrective for bureaucracy, therefore, is an emphasis upon public relations. It serves as a corrective through promoting decentralization, deemphasizing legalism and providing a test for action in particular cases. Undoubtedly the depression and its attendant forces has helped to bring about increased emphasis along this line. However, in many of the large corporations it is still superficial and there is much room for improvement.

CHAPTER VIII

PERSONNEL FACTORS

The provision of progressive management.—The following discussion of good leadership as a managerial corrective of the evils of bureaucracy is primarily concerned with direct attacks on the deficiencies of leadership as they exist and as we have described them in a previous chapter.[1] Inspiring leadership is, of course, a potent corrective for the ills of bureaucracy in the large enterprise. Indeed, it is probably the most important element in the determination of the objectives and the tone of the whole corporation. A large company may, because of other factors, exist for awhile without capable leadership, but it can scarcely be continuously successful with such a lack.

The importance of leadership is recognized by both writers and practitioners of administration.[2] One vice president of a giant corporation, for example, has laid down as the most important single rule of management:

> Get a chief executive who can lead; that is, create objectives, get people to follow, possesses an uncommon sense of what to do and when. Great administration is not primarily a matter of rules—they are incidental and subsidiary to policy. It is the product of inspiring leadership, creating confidence and satisfaction on the part of employees and the public.

The capable executive is the man who has ideas, who inspires others to help effectuate them, who is able to coordinate the work of his subordinates. A few outstanding ideas often mean the difference between the signal success of an enterprise, and mediocrity or even failure. Even a cursory examination of some of the large corporations indicates their importance: serving a mass automobile market and the refined use of assembly-line methods in Ford, and supplying farmers with a variety of products under money-back guarantees in the Sears, Roebuck and Montgomery Ward mail-order houses are obvious illustrations. Indeed, the managements of some companies feel that their executives are well worth their salaries if they get one or two good ideas in a year.

An inspiring leader not only puts across his ideas but gains employee support for the continuing policies of the company. More and more it is being recognized that Mary Parker Follett and Ordway Tead

[1] Chapter VI, supra.

[2] The limits of time and space preclude an adequate discussion of leadership here. Among the many publications which have been written on the subject are: Ordway Tead, The Art of Leadership and Human Nature and Management (New York: Harper, 1935 and 1929); Mary Parker Follett, Creative Experience (New York; Longmans Green, 1924); T. N. Whitehead, Leadership in a Free Society (Cambridge. Mass.: Harvard University Press, 1936), and "Leadership Within Industrial Organizations," Harvard Business Review, XIV (Winter, 1936), pp. 161-171; Marshall E. Dimock, Modern Politics and Administration (New York: American Book Company, 1937). Chs. X and XI; Paul Pigors, Leadership or Domination (Boston: Houghton Mifflin, 1935); F. W. Taussig and C. S. Joslyn, American Business Leaders (New York: Macmillan, 1932); E. S. Bogardés, Leaders and Leadership (New York: Appleton-Century, 1934); H. C. Metcalf, editor, Psychological Foundations of Management (New York: McGraw-Hill, 1927) and Business Leadership (New York: I. Pitman, 1931); Johnson O'Connor, Psychometrics (Cambridge, Mass.: Harvard University Press, 1934); H. L. Smith and L. M. Krueger, A Brief Summary of Literature on Leadership (Bloomington, Ind.: University of Indiana, School of Education, 1933).

have been right in their contention that power with people is more important than power over people. The latter, based on position in the hierarchy and command, too often breeds resentment and bureaucratic resistance. Influence with persons, on the other hand, leads them to identify themselves with the purposes of the enterprise and elicits their eager support. Red-blooded enthusiasm then replaces bureaucratic lethargy.

The ability to coordinate also facilitates the efficient use of the enthusiasm of subordinates. Because of its varied requirements, however, few people possess this ability:

> It requires knowledge of all aspects of the undertaking, ability to see things broadly and comprehensively, facility in altering work programs and organization when necessary better to achieve objectives, success in delegating duties, sensitivity to faulty organization or processes, courage to upset existing arrangements irrespective of whose toes are stepped on, and sustained vitality and freshness of outlook.[3]

In view of these broad qualifications it is not surprising that one hears the complaint that "There aren't enough first-class executives to go around," or, from another source, "Second-rate management must often be tolerated because the supply of first-rate managers is now inadequate."[4] Because of this lack of leadership material, therefore, it is important that potential executives be deliberately recruited, trained, and advanced so as to use them to the best possible advantage.

The obvious and probably the best source of executive material is from within the ranks of company employees. A man who has worked his way up to a position of leadership naturally has some knowledge of the enterprise as a whole and a detailed knowledge of at least part of it. Moreover, the possibility of advancement has a powerful influence on morale. It facilitates identification of the worker with the executive and serves as a stimulus to greater effort. For these reasons it is desirable, when more important considerations are absent, to promote from within the ranks when the proper man is found for the proper job.

The techniques of uncovering talent as early as possible, however, must be improved and more widely adopted. Complaints such as: "Not enough promising juniors are coming along," and "The right men are not getting to the top" demand a response and a solution. Various tests and rating systems designed to reveal executive material are current, but are often primitive and the best systems are not generally in use. Improvements in the inventory of executive material are among the first needs for the conquering of the undesirable aspects of bureaucracy through outstanding leadership. E. R. Stettinius, Jr., maintains that in the trying quest for leaders—

> the crux of the situation is * * * the failure of American business management generally to introduce an orderly and methodical system for the discovery, development, and assignment of executive personnel.
>
> We have gone on the theory that the men needed—the leaders of today and tomorrow—are automatically available among the millions in industry.
>
> But how incomplete, and how largely fortuitous are the catch-as-catch-can methods that business all too frequently employs to find them! * * *
>
> It cannot be generally said that the subject of executive personnel in industry is given the attention which it deserves, either as to its recording, evaluation, utilization in current operations, availability for transfer, or as to its development or curtailment in long-range planning. This despite the fact that there is more

[3] Marshall E. Dimock, Modern Politics and Administration, p. 275.
[4] Chester I. Barnard, Collectivism and Individualism, p. 23.

at stake and more importance to an efficient technique for inventory of executive personnel than there is in routine and currently kept inventories of properties and product.[5]

An essential procedure in the advancement of talent is thus to discover the potential leaders who are already on the pay roll but who are buried in the ranks.

Wide as it is, however, the promotion source of executives is subject to limitations. First of all, some executives complain that "the men who enter at the bottom usually are dulled before they get a chance." Probably this can never be completely prevented, though it could be eased if capable men at the bottom were early identified and given special attention. But the process of identification is difficult, and it is expensive to give special attention to a large number of persons in the hope that some of them might have the requisite talents.

Secondly, employees of large corporations, even including many department heads, are often highly specialized in skills and background. This limits their possibilities as executives. Men with a broad view are indispensable for the task of inspiration and coordination which is required of a leader. A worker who is the best of his group at a lathe, for example, may completely lack the qualities necessary for the supervision and motivation of others. There may be no overlapping among the requisite skills.

The pressure for promotion on the basis of seniority may result, in the third place, in the advancement of men without outstanding merit but with long years of service. The respective claims of merit and seniority are difficult to resolve. Labor unions commonly favor seniority, largely because they feel that those with long service and membership in the union should be rewarded, because it injects an additional element of security into jobs, and because they do not trust the alternative methods of selection. But it is disastrous for a corporation to follow this policy in any wide degree. When promotion depends upon the calendar there is little stimulation for a man to use his talents to the full extent. The method thus not only advances mediocrity to places of power but in addition kills talent. Seniority may be given importance in layoffs and continued service and may also be rewarded by periodic increases in pay, but leaders are so important to an enterprise that they should be chosen solely on the basis of merit. The proponents of seniority must be satisfied with rewards which will not jeopardize the welfare of the enterprise as a whole. If merit is early discovered, promotion on that basis usually has a better effect upon morale than promotion by seniority, and in addition the best men will be placed where their talents can best be used.

Despite the shortcomings of the policy of internal promotion, the company's employees are the most important single source of potential leaders. As we have remarked, it is a field which has not been adequately exploited, although some concerns have approached it in a fairly systematic manner. Several of the largest, for example, have rating systems whereby present and potential executives are appraised, usually by their superiors though sometimes by their peers as well. If a man rates consistently high he is investigated for promotion. In addition, of course, the usual method of watching men who have been successful in cutting expenses, increasing net revenues, or otherwise making a good record is also used.

[5] E. R. Stettinius, Jr., op. cit.

In general, however, the little that has actually been done merely serves to highlight the need for considerable refinement of current methods. Improvement would probably bring about a corresponding decrease in promotions on the basis of seniority or influence. Recognizing the need for merit at the top, one corporation official contends that progress in the quality and character of corporate organizations will depend chiefly upon the extent to which executives are intelligently selected for their work, and cease to attain positions, as they have in the past, largely by chance or pull.[6]

Even with these improvements, the company's ranks are probably not sufficient for the needs of leadership in industry. It is a healthy thing to keep the channels of promotion open from bottom to top, but there is little doubt that a high level of leadership is equally dependent upon other sources of recruitment. Executives with broad as well as specialized backgrounds are required. It is difficult for a man to rise from the ranks by his own efforts and to obtain the required breadth of vision in the process. Special sources of recruitment and special methods of training are therefore indicated.

In some respects the executive is analogous to a queen bee. Some bee larvae develop into drones regardless of the diet on which they are raised. However, whether other larvae develop into workers or into queens depends upon whether they are fed a plain or a special diet. Similarly among corporation employees only a limited percentage is potential executive material.[7] These few, however, must be fed a special diet in the form of background and training, especially while they are sufficiently young to profit by it, in order to become effective leaders. Otherwise, while they may remain good workers, they will not develop the necessary qualities of the first-rate executive.

In recognition of this need, some of the large corporations have adopted special procedures which are designed to obtain men with the desired background. Training schools, for example, have been established which employees with interest and initiative may attend and learn of matters beyond the confines of their own narrow jobs. More commonly, however, executives in the large companies are recruited from the colleges and technical schools. In this way, much of the broad training and a correspondingly valuable attitude of mind has already been acquired by the candidate before he is hired. Some officials state that not only do they obtain their executives in this way but that they prefer the smaller colleges, whose graduates are likely to be less specialized than those of the large universities.

This practice of recruiting potential executives from the colleges is widespread among the giant corporations. For example, the personnel director of a Nation-wide corporation employing over 100,000 persons, observed in an interview that there were only a couple of outstanding, up-and-coming young men in that concern who did not have a college education. One company has hired as many as 3,000 college men in 1 year. They naturally wish to keep these men on a permanent basis, for the expense of recruitment and the investment involved in special training is high. One executive commented that out of 400 college recruits in his company, 85 percent had been retained, 10 percent were failures and only 5 percent which they

[6] Malcom C. Rorty, "Men Not Things," Bulletin of the Taylor Society, XV (April 1930), p. 99.

[7] Chester Barnard estimates that not more than 10 percent of the population has the potentialities for managing affairs. Collectivism and Individualism, p. 24.

wanted to keep had gone elsewhere. These college men are commonly started at the bottom of the hierarchy but advancement may be rapid. In this way specially qualified recruits are brought into the corporation and are trained by experience in a number of lesser jobs, retaining the time-tested system of starting at the bottom and working up.

Small companies also serve as a source of executive material for the larger concerns. Here potential leaders may gain a broad background in a relatively short time. Many executives in the large corporations who have themselves come from smaller concerns, however, prefer to develop their own talent, starting with relatively young men. Moreover, it is undoubtedly good for morale to recruit from within the company when possible. Nevertheless, when fresh, red blood is needed, managers should not hesitate to go outside the company to get it. It may have a healthy, rejuvenating effect which will help to offset stagnation. They should also draw on outside men when there are no qualified candidates within the enterprise. One of Henry Kendall's 10 commandments for the cotton industry is capable of rather wide application: "Thou shalt exalt competency of management before all else, and welcome young red blood into the industry, to do things, not the way they always have been done but in the one best way." [8] In other words, neither door to promotion should be closed.

Once a young man has been taken into a company the process of turning him into an executive has just begun. His natural qualifications must be supplemented and developed through a program of training.

The training of executives takes various forms. In those corporations where serious attention is paid to the process, the general pattern is somewhat as follows: The recruit is usually given at first a simple job at a small salary. Supplementing this may be a series of informal conferences on operating and administrative problems. Regular courses have often been dispensed with, partly because the recruits have just come from college or the company training school and are weary of classes. Varied experience is then provided by assigning the men to a series of small positions in order to give them background and to discover further their special likes and qualifications. Finally they are placed in posts of some degree of responsibility and it is up to them to demonstrate their capabilities.

In some companies this tour of duty idea is continued even after the men have reached responsible jobs. In addition, allowing ambitious and capable executives a considerable degree of discretion and responsibility helps even those who are already on the way up. Statements such as "Nothing so much develops individuals within the limits of their capacity as responsibility," and "Local managers should be permitted to make mistakes; what we're interested in are results; if they've got the stuff they'll deliver under such a system," illustrate the faith of some managers in the efficiency of freedom of action in developing executive material.[9] As one corporation official has said:

> Experimentation and change always cost money, but a skilled executive will always permit an occasional experiment to be undertaken, even though in his

[8] Given before a convention of the National Association of Cotton Manufacturers and reprinted in the Christian Century, XLVII (July 30, 1930), p. 941.

[9] See also W. J. Donald, Handbook of Business Administration (New York: McGraw-Hill, 1931), pp. 1499–1501.

own opinion it is clearly foredoomed to failure, rather than have the impression spread throughout the organization that no suggestions for changes in methods will be welcome.[10]

Both increased interest and valuable training can also be acquired by promising young men if they are allowed to share, if only in a limited manner, in the determination of corporation policies. Some of the potentialities of such a plan have been amply demonstrated by trial.[11]

Despite what has been done in some instances, however, many of the large corporations may be justly criticized for paying insufficient attention to the building of executives. Through sheer inertia on the part of management, the future leader must too often take all the initiative. It is this process that so often results in having good men "dulled before they get a chance."

An additional requirement of progressive management is that promotion shall be relatively rapid for qualified men. This naturally depends upon the early discovery of talent, and, as we have already pointed out, a further refinement of the methods of discovery is indicated. Thereafter, an attitude of mind on the part of those in control is necessary in order that a promising man may be advanced before he gives everything he has to a particular job.

Rapid advancement is essential for two main reasons: First, men with unusual qualifications may become dulled and discouraged if confined too long in one position; and second, the many steps in the hierarchy of the giant corporation require that one who is destined to reach the top shall not be unduly delayed at any stage. If he is, he will be too old at the end and his term of office will be too short for the corporation to gain the maximum benefit from the use of his talents. An executive who is able to rise only part way might, of course, be advanced at a slower pace. But in all cases it is essential that men reach their peak of usefulness substantially prior to retirement. "Let those who can run fast go ahead," or "We keep shoving them along," are statements which illustrate the attitude of some thoughtful managers with regard to promotions.

Without exhausting the elements of progressive management it may be said, finally, that the incentives in any company must be adapted to the development of leadership. Outstanding leaders may be thousands of dollars more valuable to a company than mediocre men. Likewise monetary reward is a powerful stimulus not only because of the purchasing power of money itself but because income is an important criterion of prestige. The twin facts of worth and incentive, therefore, result in wide agreement on the proposition that capable business leaders should be substantially and liberally remunerated. There is less accord, however, as to just how much this remuneration shall be and in what manner it shall be paid.

Some interesting questions may be raised. For example, is the head of Lever Bros., soap manufacturers, or of International Business Machines each worth over twice as much to his company as the head of the world's largest private corporation, the American Telephone & Telegraph Co., is to that company? No one can contend that the salary of the last mentioned, over $200,000, is not substantial. Or

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[10] Malcom C. Rorty, op. cit.

[11] See Charles P. McCormick, Multiple Management (New York: Harper, 1938), for a description of the plan used in his company. For a summary, see his "Multiple Management," Society for the Advancement of Management Journal, III (January 1938), pp. 38–39.

again, can the contributions of leaders be at all accurately determined? The profits of an enterprise are commonly considered a good indication of managerial proficiency, but profits are probably still more dependent upon general business conditions. Many executives have worked harder and contributed more to their companies during the depression, when profits were meager or absent, than they did in more prosperous times. "Executives are customarily paid for exercising good judgment, formulating broad policies, and making other immeasurable contributions." [12] Because of these and similar factors, therefore, incentives directly related to what is desired of an executive are difficult to determine.

Thus, a primary need is the development of criteria for measuring executives' contributions. F. P. Poole has found, for example, that the frequent lack of even essential operating statistics was responsible for many makeshift compensation plans.[13] But even under the most objective plans that might be developed, a subjective appraisal is equally necessary in order to evaluate an executive's relative worth.

A number of companies have adopted special bonus plans to stimulate their executives. Profits serve as a common criterion of extra compensation, but are widely supplemented by appraisals of worth on other bases varying from fairly simple percentages of quotas or performance standards to rather vague judgments on "special services," "industry and fidelity," or "outstanding service." Indeed, in some companies regular salaries plus bonuses are so substantial that favored managers may become millionaires.[14]

The managements of other concerns feel that bonuses are not particularly desirable. Executives comment:

> Enormous executive bonuses are utterly inexcusable. They were the "growing pains" of industry. They were paid at a time when everyone was trying to take all he could while the taking was good.

or again—

> Bonuses are indefensible. Profits are not a reflection of managerial ability to any considerable extent; they are due to general conditions—high during prosperity and low during depression. But men have to work harder during the periods of depression.

After analyzing a number of bonus plans, F. P. Poole decided that many were improperly set up. He contends that in any such plan it is essential—

> that participation should be proportionate to responsibility. In any business, the performance of one individual may affect the results of his division only, while the performance of another may affect the business as a whole. The choice of the plan should be influenced by this consideration. * * * The reward for each should be mostly in terms of factors over which he has positive control. For this reason, profits should rarely be one of the base factors for any but the highest executives.[15]

In his list of factors to be considered in granting extra compensation at various executive levels, most of the items are not based upon profits. Perhaps the most interesting part of his study is his con-

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[12] John C. Baker, Executive Salaries and Bonus Plans (New York: McGraw-Hill, 1938), p. 236.

[13] F. P. Poole, "How Much is an Executive Worth?" Factory and Industrial Management, LXXX (November, 1930), p. 937.

[14] For example, in discussing Du Pont bonuses Fortune says: "The Du Pont man who rises high enough to be in touch with the members of the family—to be almost a member of the family—may become a management millionaire. Just as the same possibility exists in General Motors, with its strong Du Pont and Raskob influence." Fortune, X (December 1934), p. 188. For a discussion of salary and bonus payments including their relation to income of classes of large corporations and of specific corporations, see John C. Baker, op. cit.

[15] F. P. Poole, op. cit., pp. 938-939.

clusion, at which he arrived only after sympathetically examining many plans:

> The greatest value of the executives' bonus plan comes, not from the incentive feature, but from the fact that, if properly devised and set up with the right determinants, each executive visualizes the vital factors of his job more clearly, and thinks and acts along correct lines.[16]

This supports that group of managers who believe in establishing control systems along the lines mentioned earlier in this chapter, and then giving their executives security and reward through promotions and appropriate salaries. But it is only a small group. The wide variations which exist in executive compensation in the different companies indicates a lack of settled and well-considered plan.

In any case, it is widely recognized that the bonus is only one of the several stimuli which may bring out a man's qualities of leadership and aggressiveness. Financial encouragements are probably the most important, at least to a certain point. But some executives believe that "the financial incentive shrinks relatively the higher up you go." Other stimuli play a part at all levels. Several executives maintained, for example, that fear was one of the most powerful spurs to improved management and vigorous effort. "There is no sentiment or humanitarian regard in the ——— business," one official remarked. "Fear is the chief incentive. Men produce because otherwise they go out." In comparing the relative potencies of fear and bonuses, John Baker comments:

> It is doubtful if the disappearance of bonus payments between 1931 and 1935 in anyway affected the work or interest of executives, many of whom broke physically under the terrific strain of the period. It is also doubtful whether the largest bonuses ever drove officers to work so hard or created such interest as did the disappearance of earnings and the fear of failure of their companies during the period of the great depression. * * * In periods of little or no earnings, executives may be making their greatest contributions to corporate success and in such periods bonuses are not typical.[17]

Other incentives are equally important. William James observed years ago, for example, that rivalry does nine-tenths of the work of the world.[18] Rewards and measurements of performance in other than financial terms can direct this force into nonmonetary channels. Many of the greatest corporation leaders appear satisfied so far as money is concerned and crave personal distinction instead. Honors, therefore, have a place on the list of incentives. Men also desire to work for groups that are "doing things." Perhaps the best proof of this is the flood of talent which was placed at the disposal of the Federal Government in the crises of 1917 and 1933. A corporation with an aggressive program can open up well-springs of initiative which are closed to less intrepid concerns. Pride of craftsmanship—doing a good job—is as prominent a factor in the make-up of an executive as in that of an old furniture maker. A good system of measuring performance will take advantage of this force and point to the elements of a good job. Loyalty to a superior, a group, or a company also plays its part. Executives will work hard for men they like and respect. They become more easily attached to people than to ideas or inanimate symbols. Because of this an official who earns the respect—perhaps one might say the affection—of his subordinates is able to command a performance which would otherwise remain

[16] Ibid., p. 939.
[17] John C. Baker, op. cit., pp. 221, 236.
[18] William James, Psychology, vol. II (New York: Henry Holt, 1925), p. 409.

dormant. Likewise a man will work for his particular group if there is a strong bond among its members. This is also true, though probably to a less extent, for the members of a corporation as a whole.

Finally, we should mention an incentive device which unfortunately is only too rarely used in business. It is part of the control system but deserves special mention. In some companies a record is kept of the fate of the subordinates of particular officials. It is recognized that an important aspect of an executive's job is to develop the staff he supervises. If good men become buried, it is a mark against his record. If, on the other hand, they become executives themselves, the role of their superior in training them is recognized and considered in promotions, raises, or other methods of reward. This helps to provide the company with a steady stream of leaders and counteracts the all-too-prevalent tendency to confine good men to inferior positions so that their talents may be reflected in the favorable performance records of their respective chiefs.

From this cursory survey of executive resources and incentives, several things are apparent. These resources, essential and limited as they are, do not receive the attention they deserve. Efficient methods are available and should be more widely adopted. Promotion from within on the basis of merit, and special recruitment from colleges and smaller companies, should be judiciously fused to maintain a steady supply of qualified men rising to the top. Training systems should be more universally established in order to develop the qualities of potential executives. Advancement should be sufficiently rapid for men to reach their peak positions while they retain the spark of enthusiasm and invention so essential to inspiring leadership, and they should remain in these jobs long enough to make full use of their capabilities. Monetary and nonmonetary incentives are many and varied. Much room for improvement lies in eliminating the wastefulness of poorly developed monetary incentives and in making better use of supplementary stimuli. Care should be taken, however, lest the latter become an excuse for withholding adequate financial reward. Leadership is so essential in the fight against the undesirable effects of bureaucracy that all available administrative means should be employed to develop it.

The attainment of high morale.—Closely related to the problem of insuring effective leadership is that of creating and maintaining a high level of morale among the rank and file of employees. The measure of effective leadership is enthusiastic response directed toward common objectives. Without this response, workers settle into small bureaucratic groupings of their own devising. Interest in the affairs of the company is lost along with efficiency. "Morale," said a brigadier general, "is a term which should be used to express the measure of determination to succeed in the purpose for which the individual is trained, or for which the group exists. It describes the nature and degree of cooperation, confidence, and unity of understanding, sympathy, and purpose existing between the individuals composing the group." [19]

Properly utilized, most of the managerial correctives of the evils of bureaucracy which we have discussed help to build morale. If this were not so, they would have little effect as correctives. Output can be maximized only through the efforts of the rank and file. Manage-

[19] Edward L. Munson The Management of Men (New York: Henry Holt, 1921), p. 3.

ment's duty is to see that those efforts are forthcoming, they they are directed into the most productive channels, and that they are coordinated. Since morale stimulates output and serves also as an indicator of worker satisfaction (which is of some importance in a democracy) it is essential that it be fostered. The improvements in management which we have mentioned are essential, but a more direct attack on the problem is also indicated.

Stated simply, the problem of raising morale is that of giving labor what it wants [20] in such a way as to improve efficiency, unity, and enthusiasm. Morale thus requires first an analysis of labor's desires and then a prescription to satisfy them. Without the analysis the prescription will be wasteful and ineffective. And, strangely enough, in view of current emphasis on research and the processes of cause and effect in handling inanimate things, corporate management has probably been more superficial in its corresponding analysis of human causes and effects than in almost any other phase of its duties. The improvement of personnel relations too often constitutes something to be undertaken when other matters are not pressing. As one executive put it, "Our company has failed to analyze the basic complaints and desires of labor. They have tried superficial controls without knowing what they were trying to control."

The concept of labor as a commodity or a cost of production, and of labor-union activity as somehow subversive and un-American, has clouded corporate thinking and made analysis difficult. When labor is placed on the balance sheet it is hard to see that the figures represent human beings with desires, likes, and dislikes little different from those of the managers themselves. This has been recognized by a number of men with varying backgrounds but it still has not penetrated deeply enough into the thinking of most corporation officials. The late Boston merchandiser, E. A. Filene, has said—

> It was universally supposed * * * that labor was a commodity. Nevertheless, labor could not and did not act like a commodity. It acted like human beings. It acted, in fact, from much the same motives with which employers acted, and not even the most dismal economist supposed that employers were commodities.[21]

A labor leader, Robert J. Watt, expressed a similar idea in his speech before the most recent International Management Conference:

> Labor is but a group term for working people. They are people like yourselves, with the same desires to earn a decent living for their families, in self-respecting jobs which they can enjoy. They may not be so sophisticated as executives usually are, and especially in terms of leadership our officers may appear crude in their inability to use 50-cent words to express their grievances and their programs. But you can solve our community problems only by viewing labor as a mass movement of individuals with the same sort of hopes and feelings and needs as yourselves.[22]

The working man thus wants to be "geared into the culture of our time." His desires are those prevailing in a democratic America. What, then, are some of the current desires of the people of this country which find expression and hope of satisfaction in industry?

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[20] An answer to the question "What does labor want?" was briefly given by Marshall E. Dimock in a speech before the Industrial Management Society, Proceedings of the Wage Conference (Chicago, Apr. 8, 1939), pp. 71-78. The analysis of Robert Hoppock in his book, Job Satisfaction (New York: Harper, 1935), is also of interest.

[21] E. A. Filene, Successful Living in This Machine Age (New York: Simon & Schuster, 1931), p. 20.

[22] Robert J. Watt, Labor's Aims and Responsibilities, in Proceedings of the Seventh International Management Congress (Baltimore: Waverly Press, 1938), pp. 58-61, 60.

Workers, like people in general, desire security. This means, among other things, steady employment with a minimum of industrial hazards, at an adequate wage that will provide the things that are commonly accepted in the American standard of living, without continued worry least they be cut off. On the other hand, security in America does not mean class and economic stratification. It connotes, rather, a stable base from which those with the desire may climb as far as they are able. The fluctuations in pay rolls and employment of the last decade and the extent of labor turn-over which we have examined are striking indications that security in even the first sense has not yet been attained in this country.

Security also has a less recognized psychological aspect. Like other men, laborers are by nature gregarious and tend to congregate in groups. These may vary in size from the men at a particular bench or workroom to a formal labor union. They have the natural and human desire to preserve themselves. As T. N. Whitehead has pointed out, "A group will resist any outside threat to its own integrity by withdrawing into a self-made shell, and so ceasing to collaborate effectively with the larger society around it." [23]

Management must recognize these needs of the worker for security and must use available administrative techniques to guarantee it. Regularizing work and minimizing lay-offs is one method; some form of a guaranteed annual wage such as has been adopted by a few progressive companies, is another. Guarding against industrial hazards has had a considerable effect upon morale in several industries. Some executives maintain that limiting the firing power of foremen is a great help. Techniques which place workers on a more equal plane with management in bargaining power also assist in increasing security and improving morale; recognizing and using employee groups gains cooperation and dispels fear and resentment. Improved systems of selection and training, in place of the haphazard methods which are often followed, can further security by obtaining and adapting workers who are fitted for particular jobs.

It must be understood, of course, that no corporate management either should or could provide for complete security to all workers. Incompetents must be subject to removal, or morale as well as production will suffer. Insecurity for incompetence which is accurately ascertained is no hindrance to morale and it is essential to the continued existence of the corporation. But all available methods should be employed to protect qualified workers. Few corporations have as yet achieved this goal.

In addition to the universal desire of Americans for security, there is our tradition of "getting ahead." This urge is encouraged among managers; it should be no surprise that it exists among workers. Not everyone, of course, likes responsibility and so may not seek promotion. But every worker wants more income and a share in the fruits of whatever increases in production there are. Use of the speed-up whereby added productivity goes unrewarded is naturally resented. The favorable effect, on the other hand, of a few small, periodic increases in wages for those who merit them, is sometimes surprising.

[23] T. N. Whitehead, "Leadership Within Industrial Organizations," op. cit., pp. 163–164.

Happily for management, workers are not in general insistent upon added benefits if the corporation does not have them to bestow. Showing labor representatives the balance sheet has often forestalled demands for increases which could not be met. In fact, under certain circumstances, they may voluntarily take less. For example, in 1932 a railroad president who had a reputation for fair dealing persuaded the unions to agree to a voluntary wage cut which saved the railroads tens of millions of dollars. Like most Americans, workers are essentially fair when fairly treated.

Besides security and improved circumstances, workers want nondiscriminatory treatment. A sense of equality is an important part of the American tradition. Because this is so ingrained we resent it when undeserving persons receive favors. Many discerning executives point out that it is important to treat all alike—that is, without favoritism. From the informal side, management can in part guard against discrimination by the careful selection and training of foremen. The acceptance and use of grievance committees to report cases of unjust treatment also helps. More formally, the analysis and classification of positions so that equal work and responsibility brings equal pay is of great value in preventing discrimination. Schemes to discover merit which is to be rewarded by promotion or increased pay, without placing undue emphasis upon the opinions of single supervisors, are also useful. Workers distrust appraisals which are too dependent upon the likes and dislikes of one man. Personal ratings cannot, of course, be dispensed with but they should be supplemented by objective measurements in which the workers have confidence. If they like the system, their emphasis upon seniority and other rigidifying devices can be reduced. On the other hand, management must take care less nondiscrimination becomes a rigidifying nonrecognition of merit.

Finally, there is the effect upon morale of the desire for recognition. Psychologists commonly list this as a universal urge. It is a part of our American tradition, with its emphasis on the worth of the individual. As a fundamental need, therefore, it is shared by workers as by other Americans, including management.

Labor's desire for recognition has two principal phases. First, workers want to be treated as human individuals, not as cogs or the cold costs of production. Secondly, they wish to participate in the management of affairs which closely affect them.

The first is a simple enough desire. We all want appreciation, to be known by name and face rather than number and job. The worker knows he is as human as his supervisors—that he is more than a commodity or a machine—and resents the fact that others sometimes forget it.[24] Some observing managers state that "it helps out enormously in handling personnel if you personally know the employees." Even so simple a thing as calling a man by name warms his spirits and raises morale. The head of a large enterprise cannot, of course, know all the employees in the company. He can, however, see that the personal touch prevails, that foremen are not Legrees, that executives are not a species apart, that personal problems are handled in a personal way. Sincere democratization of attitude is essential to

[24] Despite their limited extent, the Western Electric experiemnts clearly illustrate the importance of human responses on morale and productivity. For a summary of these see L. J. Henderson, T. N. Whitehead, and Elton Mayo, "The Effects of Social Environment," in Gulick and Urwick, op. cit., ch. VII.

high morale in American industry. Power *with* is more satisfying and in the end more productive than power *over*.

The second aspect of recognition, participation in management, causes some trepidation among executives who do not recognize its true nature. Businessmen are understandably and justifiably resistant to any attempt to divide and diffuse the unity of management. What they sometimes fail to realize, however, is that workers do not as a rule wish to assume any such responsibility. What they do want is that their viewpoint be considered when policies are formulated and decisions reached which are of immediate concern to them. They desire cooperation rather than control. Friedrich and Cole, in their monograph on bureaucracy, have aptly said:

> To repeat here a fundamental if somewhat platitudinous truth, a group of human beings is not willing, except in certain cases of extreme emergency, to be treated like dumb animals. Whether or not their material "interests" are taken care of a little better or less well does not matter to them in comparison with whether they feel that they have had a chance to participate in deciding what those material interests are.[25]

Moreover, convinced that they have had a part in creating the profits, they wish to share in whatever prosperity the company may enjoy.

Mutual confidence rests upon an exchange of information and viewpoints and upon the belief that the other side will play fair. As one corporation executive has pointed out, "The best way to get labor's confidence is to show them the books. Most average businesses earn only a small margin, if any. Smart employers will make this fact known." If management and labor are each educated in the viewpoints and problems of the other, the result will be a workable collaboration rather than mutual recrimination and loss of morale. The cash dividends of as simple and costless a thing as a constructive, understanding attitude may be surprising. With cooperation, the objectives of the company become the objectives of all who work for it. Thus, with enthusiasm and singleness of purpose, the shackles of bureaucracy may be broken and the personnel as a working whole may become truly efficient.

Wise management will recognize these potentialities. It will take advantage of its peculiar position to initiate programs of cooperation. For, as a labor leader has aptly said—

> Management can determine the sort of leadership which Labor provides because you determine whether we must plead our cause by force or by reason. Give us conference table discussion of honest issues and you will get that kind of leadership. If you give us the Mohawk Valley formula, you will get militant unions with fighting leaders. If you give guns and gas to meet our grievances you will get the sit-down strike and the flying squadrons. You cannot breed respect and confidence by the stool pigeon and labor spy. Every union which you smash by force and deceit will be succeeded by a tougher, harder union ready to match itself against your tactics."[26]

Cooperation counteracts the ills of bureaucracy and pays dividends, particularly over the long run.[27] Conflict is divisive, wasteful, destructive of morale, and productive of a sullen bureaucracy

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[25] Friedrich and Cole, op. cit., p. 88.

[26] Robert J. Watt, op. cit.

[27] The mutually profitable, cooperative labor-management relationship of the last quarter century between Hart, Schaffner & Marx and the Amalgamated Clothing Workers is a case in point. The head of the union has pointed out that "American industrialists may well look to this record of uninterrupted, regulated industrial relationship, with not a single strike or otherwise upsetting disorder, as a harbinger of what the future has in store for us if only we determine to set reason above atavism."——Time, XXIX (April 19, 1937), p. 78. For a recent detailed statement of the potentialities of labor-management cooperation, see Morris L. Cooke and Philip Murray, Organized Labor and Production (New York: Harper, 1940).

Basic to good morale and its benefits is the attitude of mind which employers must assume. They must think of workers as human beings like themselves—not costs, commodities, cogs, or even pets. As Ordway Tead has said, "Our Koehlers and our Hersheys of varying degrees of paternalistic kindliness, must surely have come to see that theirs is no adequate answer to what the human spirit seeks in our day in our land." [28] Good management does not need to be soft—in fact, it would lose labor's respect if it were—but it does need to be human.

In order to improve morale and thereby counteract the undesirable effects of bureaucracy, management, then, needs to recognize what the actual desires of workers are, to provide as much security for meritorious men as is feasible, to allow labor an opportunity for advancement either through promotions or moderate increases in pay, to treat workers justly and without illogical discrimination, and to recognize that they are human, to treat them as such, and to allow them to participate in the formation of decisions and policies which vitally affect them. It must be understood, however, that the recognition of workers as human beings is basic to all other requirements and is the foundation upon which all other policies must be built. Otherwise, sincerity will be absent and improvement in morale will not be forthcoming.

[28] Ordway Tead, "Industrial Relations 1939 Model," Personnel Journal, XVII (November 1938), pp. 160–67.

CHAPTER IX

COMPARISON AND SUMMARY

Implications for governmental bureaucracy.—Because the problems are similar, most of the managerial correctives of the ills of bureaucracy which we have discussed are applicable to both government and business.[1] In general, they can be as effective in one type of enterprise as in the other. Some methods, however, are more readily applied in public than in private administration while others are virtually useless because of peculiar handicaps which exist.

The definition of objectives, responsibilities, and authority is probably carried as far in government as in business. It is a difficult process because neither the people nor their representatives has a clear idea of the purposes of government. Nevertheless, through creative enactments and the annual budgetary process, considerable clarity of definition may be and is in practice attained. The periodic re-examination of policies and practices, however—preventive maintenance applied to administration—is at least as rare in government as in business, although the potentialities of this technique are high in either field.

Standard practices and instructions are of course used both in government and in business enterprises. In government, however, there is even more emphasis upon legality—the necessity of following rules—than in business. This preoccupation with legality, often at the expense of effectiveness, is an outstanding characteristic of public administration. Lawmakers are more often lawyers than members of any other calling, and it is natural that they should emphasize rules. There is more joy among the opposition over one instance of doubtful legality than over 99 cases of inefficiency. This makes it difficult to give results their proper importance.

Aside from the rigidity which accompanies it, legality makes effective decentralization difficult. Although our Federal system allows a considerable degree of decentralization, many small matters must still be referred to the central office.[2] Some change in emphasis is indicated, therefore, if the bureaucratic pressure of legalism is to be counteracted.

Government might also improve its methods of internal coordination and control. The profit measure of efficiency is largely absent here, but other devices are available. A considerable portion of governmental activity, particularly that of a routine nature, may be reduced to units and measured.[3] This method cannot be carried so

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[1] Our purpose here is merely to emphasize the generic character of bureaucracy. Comparison is the best method of making common characteristics stand out. No attempt will be made to deal in detail with bureaucracy in government.

[2] Cf. James W. Fesler, "Executive Management and the Federal Field Service" in the President's Committee on Administrative Management, Report With Special Studies (Washington: Government Printing Office, 1937), pp. 275–294.

[3] See the collection of papers, The Work Unit in Federal Administration (Chicago: Public Administration Service, 1937).

far as in industry, however, because of differences in the types of work performed. The over-all cost of government, for example, is of little value in appraising its worth or efficiency. A police force on a small budget may do a very poor job of law enforcement.

Internal coordination in government could be substantially improved if there were more continuity of leadership at the upper levels. A rapid turn-over at the top has the effect of segregating the various subdivisions, thus preventing their integration into a unified whole. Less volatility of leadership would help to build a system and habit of unified, cooperative action.

The technique of public relations can be as effectively applied in government as in business. The tradition that it is undignified or even dangerous for government to recognize public desires and to advertise its own merits is disappearing, and experts on public relations are coming to be regularly employed.[4] This is but one aspect of a growing appreciation of the importance of public satisfaction. The emphasis could be extended to the inner portions of the governmental bureaucracy with beneficial effects. The public-service incentive is strong but it needs to be expanded, channelized, and supplemented by other direct emphases.

Government should likewise improve the caliber of its managers. In order to attract and hold good men it must continue to be an agency which is "doing things." It must also pay higher salaries to men of exceptional capabilities. This would tend to put a stop to the present business practice of buying outstanding talent from governmental units which badly need it.

In improving morale among the rank and file of employees, government could make the surest advances through a fundamental change in its attitude toward personnel work. The negative emphasis of "keeping the spoilsmen out" should be shifted to one of attracting, developing, and keeping good men in. It is personnel work beyond the recruitment stage which should be given emphasis. This shift in attitude would include the adoption of a number of improved personnel practices which we cannot here discuss.

Many of the techniques which are available to business in counteracting bureaucracy are thus also available to government. It too can benefit from a clearer definition of objectives, the application of preventive maintenance to administrative policies and practices, the stressing of results, improvements in devices and underlying conditions of effective coordination and control, decentralization, an emphasis upon public relations, provision of more capable managers, and the adoption of attitudes and practices directed toward improving morale. Just as the problems are largely similar in government and business, so also are the solutions.

Nevertheless, in some respects government is more hampered than business in the application of correctives to the undesirable effects of bureaucracy. There are the several traditional and organizational handicaps which we have mentioned, such as a lack of emphasis on administrative unity, the separation of powers which promotes jealousy among branches of the government, the fact that each bureau has its own supporting clientele, an undue emphasis on legality, and low salaries coupled with insecurity of tenure for men at the top. In addition, in State and local governments the direct election of many adminis-

[4] See James L. McCamy, Federal Publicity (Chicago: University of Chicago Press, 1939).

trative officers often deemphasizes the need for coordination among them. Finally, the variety of governmental work results in the creation of an organizational structure with so many units at each level that one executive cannot effectively coordinate the activities of his too numerous subordinates.

On the other hand, government also has advantages which business does not enjoy. It is able, for example, more readily to utilize certain incentives which strongly appeal both to leaders and to the rank and file. The elements of prestige, of appeal to service and patriotism, and of belonging to an agency that is "doing things" (or, at least, has been for the past decade), serve in large part to counteract the handicaps of lower salaries and shorter tenure for the top men. These same incentives apply also to the rank and file. In addition, it is easier in government to promote security, nondiscrimination, and better hours, wages, and working conditions at the lower levels of the hierarchy. They fit in with democratic tradition.

Thus in the application of correctives for the ills of bureaucracy, government has both handicaps and advantages when compared with business. Although the net result is difficult to determine, it is probable that the handicaps of government are slightly greater than those of business, though there are many exceptions. A device such as the government corporation which can draw on the useful traditions of both government and business holds some promise in counteracting bureaucracy, particularly in the provision of economic services.[5] It is clear that the successful application of antidotes requires not only the direct use of appropriate techniques but changed traditions as well.

Summary and recommendations.—The factors contributing to the evils of bureaucracy are numerous and varied; so also are the administrative antidotes with which to combat them. The problem is so complex and pervasive that no simple, single remedy is adequate. While it is true that some correctives have rather general effects, others have quite specific results. Although in our discussion of these remedies we have not exhausted the list, we have mentioned those which are the most important and are capable of the broadest application.

The unresponsiveness, divisiveness, and inflexibility of business bureaucracy may in part be corrected by the various means which we have considered. A reasonably clear definition of objectives, responsibilities, and authority will help to direct the efforts of all members of an enterprise toward common goals and to minimize the confusion and jealousies resulting from hazy conceptions of who is to do what. The attitude, "We don't know where we're going but we're on our way," must be supplanted by a clear knowledge of goals and spheres of activity.

Ossification of administrative methods and goals could be largely prevented by a thorough, objective reexamination of them at periodic intervals instead of only in times of crisis. The idea of preventive

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[5] A rather considerable body of material on the government corporation has been built up in recent years. For a discussion of the subject see, among others, Marshall E. Dimock, "Principles Underlying Government-Owned Corporations," Public Administration, XIII (January 1935), pp. 51–66, "Public Corporations and Business Enterprise," Public Administration, XIV (October 1936), pp. 417–28, British Public Utilities and National Development (London: Allen and Unwin, 1933) and Modern Politics and Administration (New York: American Book Co., 1937), ch. XIII; John McDiarmid, Government Corporations and Federal Funds (Chicago: University of Chicago Press, 1938); John Thurstone, Government Proprietary Corporations (Cambridge, Mass.: Harvard University Press, 1937); Terence O'Brien, British Experiments in Public Ownership and Control (London: Allen and Unwin, 1937); Lincoln Gordon, The Public Corporation in Great Britain (London: Oxford University Press, 1938); H. A. Van Dorn, Government-Owned Corporations (New York: Knopf, 1926).

maintenance may be applied to administration as well as to machinery, and with equally desirable results. But the constant attention of specialized staff men as well as of regular executives is indicated if such a procedure is to be effective. A half-way job may only cause additional confusion.

The use of standard practices and other rules which represent as nearly as may be the "one best way" is to be commended as an element of efficient administration. Nevertheless, if flexibility is to be maintained, emphasis must be upon results rather than upon blind obedience to regulations. Excess legalism not only destroys personnel interest but introduces an extreme form of bureaucratic inflexibility which is always inefficient. Rules must be recognized as merely a means to certain ends. To insure this attitude there must be a well-formed and widely understood conception of the aims of the enterprise.

Improved methods of coordination and control also counteract unresponsiveness and inflexibility. The development and use of unit measurements of performance, in monetary, as well as in nonmonetary terms, merits wider application. Informal contacts across hierarchical lines and the use of interdepartmental or interdivisional committees provide effective means of coordination which short cut the cumbersome process of referring matters solely through hierarchical channels. Flexibility is here more readily attained because adjustments can be made at the source of the difficulty. In the hierarchical structure, coordination is also furthered by restricting the number of an official's immediate subordinates. An executive's span of control is subject to limitations if he is effectively to coordinate the activities under his supervision. Indeed, it may be said that any methods which increase the effectiveness of coordination and control likewise contribute to the fight against bureaucracy, for without unity of action bureaucratic divisiveness and inflexibility inevitably result in wasted time and effort.

Decentralization of authority and an emphasis upon public relations are equally useful devices in keeping administrative methods and decisions close to the problems of the enterprise and to the customers. They thus contribute to efficiency and to a fuller satisfaction of the needs of the market.

A high level of morale is also essential to the conquest of bureaucracy. The process of its attainment may be stated quite simply. It consists essentially of giving labor what it wants in such a way as to improve efficiency and enthusiasm. Briefly, laborers want a measure of security, an opportunity to share in improved standards of living, nondiscriminatory treatment, and, basic to all, they want to be treated as human beings—as partners in productive enterprise—and to be given a voice in the determination of policies which vitally affect them. Labor is no less, and no more, fair than any other large group of men and women. It responds as all such groups do. Astute management, therefore, will seize the opportunity to increase productivity at a common cost of little more than the sacrifice of a few illogical and outmoded prejudices.

Finally, the ill effects of bureaucracy cannot be overcome without the development and full use of capable, progressive leaders. Inventive men who can conceive and plan, who have the ability, disposition, and courage to put bold plans into effect—to upset routine and disturb

established relationships when necessary—and who can inspire others to unbureaucratic levels of activity, cannot be dispensed with. It is not adequate simply to hope that such leadership will arise of its own accord. Too many potential leaders are deadened before they get a chance, unless special effort is directed toward their discovery and development. Many can be recruited from within the concern itself, if merit rather than seniority or pull is emphasized in promotions. In addition, special recruitment from colleges and small companies is necessary in order to obtain new blood and breadth of outlook. But whatever the source, potential leaders should be given special training and attention in order to develop their capacities to the full. Then they must be advanced sufficiently rapidly to reach their peak positions before age overtakes them. Finally, the incentives utilized should be such that leadership is developed as well as rewarded. Leaders are of such value to the success of an enterprise that no element which will contribute to their fullest utilization should be ignored.

Bureaucracy is an important problem of big-business administration. To a large extent, however, it can be overcome by the use of the administrative techniques we have discussed. Both business and government would profit by their wider application. Such remedial action could improve the efficiency of our economic order and thereby raise our standard of living.

The nature of these antidotes, however, precludes their application as a direct result of legislative action which the Temporary National Economic Committee might recommend. Business in its own self-interest should be induced, if possible, to recognize and apply them. The committee may, however, draw attention to the problem of bureaucracy and indicate the available remedies. Administrators need to be reminded of these basic problems and possible solutions. They too easily become so engrossed in pressing day-to-day difficulties that questions of a continuing and in fact more important nature are often neglected.

In addition, the possibility of enlisting the help of the Department of Commerce in increasing the productivity of industry through preventing the wastes of bureaucracy should be examined. The Department might well be of substantial assistance if it would establish a unit to study problems of administration and to give expert advice and aid to executives who ask for it. The combined cooperative efforts of business and government could thus be utilized in a concerted assault on one of the most vexing set of problems faced by the administrators of big business. If the savings of increased efficiency were passed on, the whole Nation would benefit materially.

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PART IV

THE IMPLICATIONS OF TRUSTEESHIP

CHAPTER X

THE REQUIREMENTS OF TRUSTEESHIP

We have already shown that trusteeship and bureaucracy are interrelated,[1] for both arise when the modern corporation becomes so large that ownership is separated from control. Though related, however, they may best be individually dealt with, for bureaucracy is a problem in management while trusteeship is a problem in democracy. Both, of course, are governmental in their nature, involving power relationships, leadership, consent, and organizational structure—as Gardiner Means has said, the peculiar province of the political scientist [2]—but they present themselves from different vantage-points. Bureaucracy is largely, but not wholly, an internal manifestation, involving internal relationships; while trusteeship deals with external relationships, being the responsibilities of management toward outside groups.

What are the practical administrative possibilities of trusteeship and the methods whereby it can be made effective without the loss of counter-balancing administrative efficiency? This is our question, and, not only for the government of business but for the government of society as a whole, it can scarcely be exceeded in importance. In some ways, trusteeship is even more crucial than bureaucracy, its causes and attempted cures, for it is one of the pivotal problems of our democratic-capitalist structure.

We shall not attempt to deal with the legal and economic aspects of trusteeship, for we feel that they may be better covered by others who have already written on the subject or who are preparing special reports for the Temporary National Economic Committee. As in the case of bureaucracy, therefore, our attention will be directed to the administrative requirements and implications of our subject, which of necessity is partly in the realm of exhortation as well as partly, and perhaps fortunately, in that of practical prescription.

The point of departure is to remind ourselves that corporate managers have automatically, although not necessarily inescapably, assumed a fiduciary responsibility toward owners, their nominal masters. The present diffusion of stock and weakness of effective stockholder control create a situation closely resembling that of the ordinary trustee and beneficiary. In both cases, direction is in the hands of persons other than the owners, for whose benefit, however, the property or business is presumably administered.

In the ordinary trust relationship the law has established certain broad requirements. In regard to trust companies, for example—

the law seeks to emphasize the sacred and binding character of a trust; hence it does not permit the trustee to administer the trust for his own benefit, while it

[1] Supra, pp. 3–5.

[2] Gardiner C. Means, "The Distribution of Control and Responsibility in a Modern Economy," in a symposium edited by Benjamin E. Lippincott, Government Control of the Economic Order (Minneapolis: University of Minnesota Press, 1935), pp. 1–17, 8.

requires him to use reasonable care to act in accordance with the terms of the trust instrument, under liability of an action at law by the beneficiary.[3]

The analogy is there, but the implications are not parallel, for in the case of corporate trustees the limitations on action have not been correspondingly extensive. If, for example, by reason of its position, management can without deception but equally without disclosure, take advantage of a shareholder without depleting the corporate assets, he may do so.[4] Despite the legislation of recent years, there remains considerable opportunity to distribute potentially profitable transactions, such as purchases and sales, on bases which include favoritism. Managers can also use their positions of power to obtain high salary and bonus rates. These are but two of the many ways in which management may turn power into private profit. "The trouble with our company is that it needs to take the dollar sign out of its symbol," said one business official; "the executives work only for money and hence not for the corporation."

With the separation of ownership and control, either businessmen must be instilled with a voluntary and effective sense of trusteeship, or society must discover means wherewith to make trusteeship effective. A realist will not rely upon either means alone. It is the part of statesmanship to make them coalesce.

Belief in the efficacy of voluntary trusteeship may appear sanguine, but there is at present no alternative when corporations become so large that the market loses much of its effectiveness as a regulator. The primary argument in support of private capitalism when it was throwing off the shackles of mercantilism was that competition, like an invisible hand, would guide economic activity into the most productive channels. Competition was to be society's protection against profiteering and other unscrupulous practices, and was also to provide an opportunity for the exploitation of inventions both in methods and materials. The market was to serve as arbiter of the claims of rival merchants and customers. Such a plan might work in a simple economic society composed of many small, independent enterprises, but with the growth of big business the market loses much of its potency as a regulator. Indeed, today many of its functions have been taken over by administrators of the giant corporations.[5]

Now we have a situation wherein society has granted certain economic liberties while relying upon the market for protection against their abuse. With this protection substantially curtailed, it is necessary that other instruments of regulation be discovered and applied.

Recently there has been increasing evidence of a vague awareness of broad responsibility on the part of corporate management. An examination of the annual reports of some of the large companies for the past few years reveals that frequently a section deals with corporate responsibility to various groups. Those most often mentioned are the investors, labor, and consumers or the public. Sometimes government is also included. The responsibilities commonly alluded

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[3] W. H. Steiner, "Trust Companies," Encylcopaedia of the Social Sciences, XV, p. 110.

[4] See Berle and Means, op. cit., pp. 221, 226. This freedom to "milk" investors by the purchase and sale of stock on the basis of inside information was substantially curtailed by section 16 (b) of the Securities and Exchange Act of 1934. Under this provision, profits from sale and repurchase or from purchase and resale of the securities of a company with which the officer, director, or beneficial owner is identified, are recoverable, with certain exceptions, if the cycle of transactions is completed within a period of 6 months. Of course, this limitation applies only to securities listed on exchanges, but it is probably here that manipulation and stock transactions on the basis of inside information have been most profitable.

[5] For a fuller discussion of these points see supra, Part I.

to are the provision of a fair, adequate return on investments; fair wages and working conditions, together with some mention of regularity of employment; and a good product at a fair price. What is "fair," however, is seldom defined. It must, of course, be recognized that the mere mention of responsibilities does not necessarily assure their acceptance. Effective public relations techniques do not require the literal fulfillment of such statements. Nevertheless, once the responsibilities are admitted there is more hope of their gradual translation into conduct.

A logical analysis of the requirements and implications of trusteeship may be expected to influence the attitudes of executives. Owen D. Young has said, for example, "It makes a great difference in my attitude toward my job as an executive officer * * * whether I am a trustee of an institution or an attorney for the investor." [6] Enlarging upon this statement, he made the customary break-down of his trusteeship into that toward the investor, toward labor, and the public. He wanted his company to be so managed that capital would be readily available at all times, the best laborers would want to work for it, and the public would prefer its products. The satisfaction of each of these groups, of course, reacts favorably on the others, for as another executive has pointed out, "Responsibility to the investors is not at variance with responsibility to other groups; if you serve these other responsibilities you serve the owners better than if by not meeting those obligations you create an untenable situation." And an official of a third corporation maintains, "Our company needs a public utility philosophy; if it doesn't get one it will become a public utility."

In a practical sense, management is a broker who balances, harmonizes, and controls the demands of various interested groups and fuses the net result into a workable program of action. The weight which is given to the demands of a particular group depends upon its effective strength, plus the degree to which management feels a responsibility to it. Thus, effective trusteeship is the result of a combination of traditional obligations and adequate pressures. We must briefly examine the more important of these to which management is subject.

First, a general observation: Managers must be inventive if there is to be progress. While it is true that particular groups often oppose the introduction of new methods, products, or ideas, yet the broad interests of the larger groups are on the side of invention. It is in the interest of management itself to develop new methods whereby its tasks may be easier or its work more effective; stockholders desire the additional dividends which may be forthcoming from the development of new products or the exploitation of new markets; labor favors increased opportunities for employment and expanded production if it can share in the benefits; consumers want more and better products and services within reach of their purchasing power; government, as the agent of the people, wants prosperity and progress with fair play. An inventive, aggressive management is in a position to contribute substantially to the satisfaction of those desires.

More and more we are dependent upon large research laboratories for the development of new products and methods. Although the

[6] Fortune, III (March 1931), p. 94.

period of simple discoveries is by no means past, the most important scientific developments are becoming increasingly the products of the large laboratories, supplied with ample capital and specialists. In some respects research itself has almost become big business. Several of the largest companies have research laboratories which are comparable to the best which universities and government can offer. But much remains to be done. The chairman of General Foods Corporation, for example, has said: "I, for one, am surprised to realize that only one or two American manufacturers out of every hundred have a research laboratory. * * * We can and must do more." [7] The outer boundaries of applied science have not been reached, and it is part of the trusteeship function of business to help extend the frontiers.

But social invention is even more urgently needed than scientific discovery. Social lag is pronounced in our economic world, and potential production is far in advance of actual consumption.[8] We need aggressive inventors to open up new markets, to create distribution machinery as efficient as present production machinery. There is also much room for invention in the realms of labor relations and managerial methods. Some of the largest corporations have specialized staffs spending full time on the development of new personnel procedures, but it is only a beginning. We need more inventive minds and more encouragement and opportunity for those we have.

In an examination of the group pressures which impinge upon management, a logical starting point is the demands of the managers themselves. Without exhausting the list, it may be said that they desire income, influence, security, and some opportunity for creative expression. The position of influence which management occupies in the large corporation indicates that this aspiration at least has received a substantial degree of satisfaction. The opportunity for creative expression, on the other hand, has been hampered, but there is clearly more opportunity in this regard for managers than for the rank and file.

The managers' desire for security has also been largely satisfied, at least at the top levels. Insofar as security relates to employment, we have already noticed that the top men of some of the largest corporations have been employed by their companies for a considerable number of years. Turn-over for the top positions is not particularly large.[9] Nor were positions at the upper levels materially decreased or abolished with the onslaught of the depression. An indication of the stability of executive employment for a sample of 100 large industrial companies is presented in table XIX. For comparative purposes an index of industrial employment for wage earners is included. The relative stability of executive employment is doubtless due to the necessity of retaining key men as well as to the power which executives themselves possess. At the top levels of management, therefore, security of employment has been to a large extent attained, while in the ranks, wage earners may be dropped.

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[7] From a speech by C. M. Chester, reprinted in the Congressional Record, Tuesday, February 6, 1940, p. 1761.

[8] A number of studies of this subject have been made. For a conservative estimate see Edwin G. Nourse, America's Capacity to Produce, and Maurice Leven and others, America's Capacity to Consume (Washington: Brookings Institution, 1934).

[9] See table X, p. 46; also p. 52.

TABLE XIX.—*Fluctuation in executive employment in 100 large industrial companies and in employment of wage earners in factories, 1928–32* [1]

Year	Number of executives	Relatives (1929=100)	Industrial index of employment, wage earners
1928	941	94	94
1929	996	100	100
1930	995	100	88
1931	1,008	101	73
1932	986	99	61

[1] From John C. Baker, Executive Salaries and Bonus Plans (New York: McGraw-Hill, 1938), p. 14.

There is also comparative stability in salaries and in total executive compensation during good times and bad. John C. Baker remarks, for example, that in 100 large industrial companies, "successive reductions in 1931 and 1932 left the total (executive) salary payments only slightly below the 1928 level, about 2.5 percent. * * * We are forced to conclude that salaries of executives are highly inflexible, to the point of being almost a fixed charge upon the company."[10]

As might be expected in the depression, bonus payments to executives dropped along with business activity and profits, and under those circumstances some corporation officials had their total remuneration substantially reduced. Nevertheless, it should be noted that the basic salaries of executives who also receive bonuses are about equal to those of executives who are paid solely by the salary method. As John C. Baker has pointed out—

There is no evidence that the use of bonus plans lowered the regular cash salaries paid executives. Instead, there is definite evidence that companies paying bonuses paid larger total compensation to their officers than did non-bonus-paying companies.[11]

Thus, a reduction in bonuses did not create an inequality of remuneration.

Total compensation, including salaries and other rewards, remained relatively stable in the business decline of the early 1930's at least in comparison with such items as earnings and wage payments. Chart VIII, for example, shows the relationship between executive compensations, earnings, and dividends for 51 large industrial companies during the period 1928–36. The comparative stability of executive compensation is apparent. For a large group of corporations the Twentieth Century Fund staff found that in 1933 total executive compensation had dropped to a point 38 percent below the 1928 level, but that during the same period wage and salary payments to other employees had dropped 49.2 percent.[12]

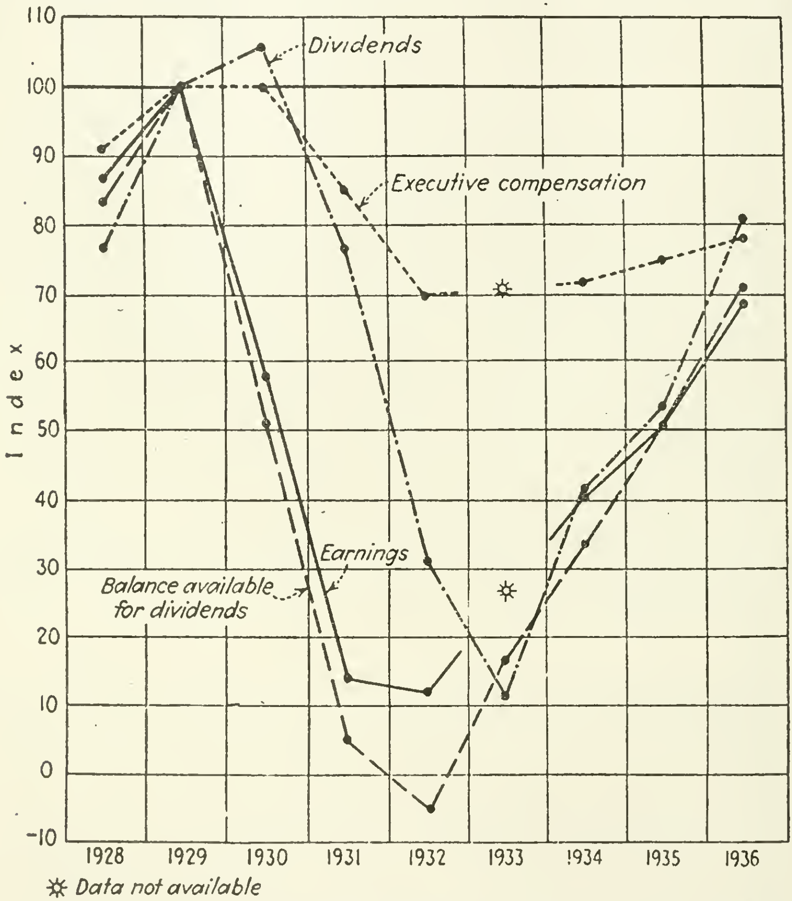
In summary it may be said that salaries—

do not vary nearly as much with general business conditions as do wages or dividends. On the whole, in good times and bad, corporate officers, as a group, fare better than wage workers or investors. In bad times, total salary payments to officers are "stickier" than wages and dividends—they go down more slowly and less far; in good times they go up faster and farther.[13]

[10] John C. Baker, op. cit., p. 20.
[11] Ibid., p. 235.
[12] Twentieth Century Fund, A Memorandum on the Problem of Big Business, p. 26.
[13] Ibid., p. 25.

Total compensation is more variable, but here also the decline during the depression was only about one-half or two-thirds as great as the decline in wage payments and much less than the decline in dividends and earnings.

CHART VIII.—FLUCTUATION IN EXECUTIVE COMPENSATION, BALANCE AVAILABLE FOR DIVIDENDS, EARNINGS,[1] AND TOTAL DIVIDENDS FOR 51 LARGE INDUSTRIAL COMPANIES: 1928–1936[2]



[1] Earnings is defined as net income after all charges including depreciation and Federal taxes, but before executive compensation and interest.

[2] From John C. Baker, Executive Salaries and Bonus Plans (New York: McGraw-Hill, 1938), p. 180.

The level of compensation indicates not only that a fair degree of security has been achieved, but that the desire of management for personal income has also received substantial satisfaction. An indication of executive compensation for 44 large industrial companies is given in table XX. The dollar figures in this table refer to the medians; that is, half of the executives in each category received more than the amount stated and half received less. While the variations

were rather substantial, the figures nevertheless give a rough, generalized picture for the group. Moreover, "large companies generally paid higher total dollar compensation, irrespective of earnings, than small companies." [14]

TABLE XX.—*Typical dollar executive compensation of 44 large industrial companies, 1929 and 1936* [1]

Ranking of executives in individual companies	Amount (median)	Percent of median compensation of highest paid executive
1929		
Highest paid executive	$101,000	100
Second highest paid executive	76,000	75
Third highest paid executive	59,000	58
All other executives (averaged)	26,000	26
Total executives (averaged)	40,000	40
1936		
Highest paid executive	93,000	100
Second highest paid executive	64,000	69
Third highest paid executive	50,000	54
All other executives (averaged)	[2] 24,000	26
Total executives (averaged)	[2] 35,000	38

[1] From John C. Baker, Executive Salaries and Bonus Plans (New York: McGraw-Hill, 1938), p. 181.
[2] These averages for 1936 are to be considered merely suggestive, since the total dollar amounts paid to executives in 1936 were in a few cases estimated for use in the study, and in many instances the total number of executives employed was not clearly stated on the Securities and Exchange Commission Form 10K for 1936.

Thus, it is obvious that average executive salaries achieve comfortable proportions.

We may then conclude that the demands of managers for influence, freedom, security, and income have met with substantial response. Because of their value to the corporations and their positions of power, the executives of the large concerns have signally registered on every score. There is little that can be recommended, other than the suggestion that it would perhaps be well to equalize some of the widest variations in executive compensation. As a group, management fares better than any other large aggregation interested in the American economy, and this is particularly true of the giant corporation.

Several related questions are immediately suggested. Have other groups fared as well at the hands of management, as management has itself? Are the pressures which these groups are able to exert sufficient to make trusteeship effective? If management were left to govern itself would the legitimate demands of these other interests be met? To a brief examination of such questions we may now turn, taking first the stockholder group.

Despite the predominant power of management, major stockholders and the managers of the large corporations ordinarily get along very well together. It is probably safe to assume that these major stockholders obtain substantially what they want if the corporation and the management have the wherewithal. Some executives feel that if there is a strong concentration of stock ownership, the desire for a "killing" is intensified. The corporation is then managed for the

[14] John C. Baker, op. cit., p. 239.

short-run benefit of the few large owners rather than for the long-run benefit of the business and the other groups concerned. Regardless of the extent to which this may be true, the large stockholders are at least better able to obtain what they want than are other nonmanagement interests.

The small, and in fact the typical, stockholder in the large corporation presents a different problem. Although he shares in ownership, power has been shorn from him. Such stockholders do not invest their money with the intention of gaining control over company policies. Theirs is what we have termed "cataclysmic control," exercised under leadership and only in periods of grave crisis. Rather, they desire a liberal, steady rate of earning. They do, however, possess a lever with which to move management. An expanding corporation must have additional funds from time to time which cannot always be provided from surplus. Hence management must so treat the rank and file of stockholders that financial aid will be forthcoming when it is required.

The large companies as a group have a more stable rate of earnings than small companies, since among the large concerns the spread between profits and losses is smaller. Whether or not the giant corporations as a group also earn at a higher rate than the various groups of smaller concerns, appears, on the basis of available data, to be an open question. The Twentieth Century Fund staff has found, however, that if appreciation in the value of stock is considered, a widely spread investment in the largest companies would have resulted in a satisfactory rate of earnings. For the period 1931–33, for example, they found that corporations with assets of $50,000,000 or more constituted the only group which showed a net profit for each of these 3 years. To a considerable extent, however, this may be due to differences in the capital structure of the large and small concerns. Giant corporations usually have a higher proportion of common stock and thus a lower proportionate fixed charge against earnings. In addition, the large companies paid more regular dividends through the depression because of accumulated surpluses on which they could draw.[15]

In general, then, it may be said that the giant corporation substantially satisfies the stockholders' desire for security. Likewise, earnings over a period of time compare favorably with those of other enterprises, particularly when increases in the value of stock resulting from accumulated surpluses are taken into account.

Some large companies could occasionally pay higher dividends through a decrease in other expenditures. It is not necessary, for example, to pay large bonuses in addition to liberal salaries in order to spur executives to their full effort and ingenuity. As we have pointed out, bonus payments among the large companies have not generally been used instead of salaries, but in addition to them. Thus, John C. Baker comments: "On the average, the chief executive who received a bonus also was paid a salary within a few thousand dollars as large as a president who was simply paid a fixed cash salary." [16] While Baker found in his study that executive compen-

[15] For data in support of this paragraph see the Corporation Survey Committee, How Profitable Is Big Business? (New York: Twentieth Century Fund, 1937) and A Memorandum on the Problem of Big Business.

[16] John C. Baker, op. cit., p. 222.

sation in the large corporations taken as a whole represented a moderate percentage of earnings and sales, nevertheless—

> the variations in such payments, * * * were so wide as to raise some question concerning the policies being followed among certain companies. Whether executive payments were too high or results too meager are questions which might be asked of specific companies. Statistically no significant relationship or correlation could be discovered between executive compensation and earnings.[17]

Savings in executive bonuses could be properly diverted to stockholders or reflected in benefits to other groups. In the giant corporation, however, these increases would be quite small, because executive compensation does not constitute so large an item as dividend payments. During the period 1928–36, for example, shareholders of a sample of the large corporations received on the average some 14 times the sums received by executives.[18] Obviously any reduction in bonus payments would represent but a small part of the total compensation of executives and a much smaller part of dividend payments. Nevertheless, in specific companies the benefit to stockholders might be substantial.

Savings to investors could be promoted in other ways as well. It is, of course, impossible to estimate the extent to which the so-called borrowing of funds by executives such as Richard Whitney, or the late F. D. Coster (or Philip Musica), formerly of the McKesson & Robbins drug firm,[19] has been and is carried on. The fate of these men may give others pause. In any case, trusteeship demands that such practices be eliminated.

Without exhausting the list, we may mention, finally, losses to investors arising from poor business judgment. It is naturally too much to expect that business leaders shall direct the affairs of large corporations without erring, but many of the more serious mistakes of judgment could be prevented by adequately gathering and using available information. An expansion of corporate research facilities is, therefore, indicated, as well as an open mind on the part of those who make the major decisions.

Among instances of mistaken judgment there is a group that is particularly important in a discussion of trusteeship. These are the cases where business judgment is at least partially blinded by the prospects of possible advantages accruing to management or those in control. The Insull utility empire is an example. Here legal as well as actual power was concentrated in the hands of Samuel Insull and his associates, despite a proportionately small investment on their part. Under an expanding economy the rewards were large, but the process of financing by issuing senior securities to the public and retaining the voting paper created so inflexible a pyramid that it could not adjust to a decline in economic activity. Here it was poor judgment plus an imperfect sense of trusteeship on the part of those in control that caused such disaster to the investors' interests.

Excessive salary and bonus payments, occasional dishonesty, poor business judgment, and the use of the corporation for private ends are ways in which potential benefits to stockholders are lost. Stockholders cannot often remedy such faults, because their power is so

[17] Ibid., pp. 183–184.

[18] Ibid., p. 157.

[19] See New York Times, March 9, 1938, et seq., especially the issues of October 28, November 1 and 2, which give a summary of the Securities and Exchange Commission report on the *Whitney case*. For the *Musica case*, see "McKesson & Robbins: Its Fall and Rise," Fortune, XXI (March 1940), p. 72.

diffused. They might, of course, create effective pressures by demanding more information and responsibility than they now have, and they might also make additional use of the instrument of government. By and large, however, the stockholders of the giant corporations have little of which they can complain. The requirements of security and liberal returns on invested capital are largely met by the managers of these concerns.

Management trusteeship is also directed toward labor. With the growth of the factory system and the loss of face-to-face contacts, management's responsibility regarding the desires of labor suffered a drastic decline. Men, women, and children were worked long hours, and even valuable employees were, and still are, laid off instead of tided over.

The human desires of labor have been discussed in a previous chapter,[20] together with some methods of satisfying them. We have also seen that the labor record of the large companies on the whole compares favorably with that of the small ones.

In remedying the discrepancies which exist, labor now has several important instruments. The logic of enlightened self-interest on the part of management is one of these. When managers fully understand the potentialities of high morale and a curbed bureaucracy, remedies such as we have discussed will be more widely applied. In addition, recent laws help to correct some of the more flagrant violations of the needs and rights of labor. The Social Security Act, for example, helps to satisfy the desire for security; the Wages and Hours Act puts "a floor under wages and a ceiling over hours" for millions of workers; the National Labor Relations Act guards labor's right to organize and bargain collectively. These and other statutes of long standing, such as the workmen's compensation acts and other regulatory measures in the various States, provide a legal basis for equitable relationships between management and labor.

Furthermore, the bargaining power of labor has been enhanced through the recent growth of labor unions. The claimed membership is now approximately 8,000,000, and constitutes about a fourth of the employee group. The proportion is higher in the industrial sectors where the large corporations grow thickest. Labor is thus in a relatively more favorable position than in the past to exact a degree of effective trusteeship on the part of management.

There are indications, also, that management is increasingly aware of its responsibilities to labor. The acceptance of collective bargaining by such corporate giants as United States Steel and General Motors is illustrative. So also is this statement of a corporation president to the workers in the enterprise:

> It is the chief concern of the managers to try to plan for the best possible uninterrupted annual wage for both job holders and stockholders. Then neither of them will have to be laid off. Your company managers know that both stockholders and job holders are dependent upon each other, and that neither could profit without the support and cooperation of the other.[21]

Despite such advances in the building of trusteeship, there are large gaps which remain. A full recognition of bargaining equality for labor is far from realized. All too often, labor is looked upon as a commodity. Workers are not credited with the same desires, needs,

[20] Supra, ch. VIII.

[21] From the foreword by Lewis H. Brown in The Year 1937: A Report to all Members of the Johns-Manville Organization (New York: Johns-Manville, 1938), p. 1.

and feelings as managers. On the economic side, we have already noted that the salaries and employment of managers are much more stable and favorable than the corresponding items in respect to labor.

In addition, the income level of multitudes of the Nation's workers is miserably low. This is revealed in chart IX and table XXI, where the concentration of families and single individuals [22] at a relatively low income level is set forth. Twelve million of these, or nearly a third, have annual incomes of less than $750; 27 million, or about two-thirds, receive less than $1,500, or an aggregate income approximately equivalent to that of the most fortunate 10 percent. The top one-half of 1 percent obtains about the same total income as the bottom 32 percent. Moreover, economic circumstances or other considerations caused the 6 poorest tenths to spend more than their current income, more in total than the next three-tenths saved.

TABLE XXI.—*Distribution of families and single individuals and of aggregate income received, by income level, 1935–36* [1]

Income level	Families and single individuals			Aggregate income		
	Number	Percent at each level	Cumulative percent	Amount	Percent at each level	Cumulative percent
Under $250	2,123,534	5.38	5.38	$294,138,000	0.50	0.50
$250 to $500	4,587,377	11.63	17.01	1,767,363,000	2.98	3.48
$500 to $750	5,771,960	14.63	31.64	3,615,653,000	6.10	9.58
$750 to $1,000	5,876,078	14.90	46.54	5,129,506,000	8.65	18.23
$1,000 to $1,250	4,990,995	12.65	59.19	5,589,111,000	9.42	27.65
$1,250 to $1,500	3,743,428	9.49	68.68	5,109,112,000	8.62	36.27
$1,500 to $1,750	2,889,904	7.32	76.00	4,660,793,000	7.87	44.14
$1,750 to $2,000	2,296,022	5.82	81.82	4,214,203,000	7.11	51.25
$2,000 to $2,250	1,704,535	4.32	86.14	3,602,861,000	6.08	57.33
$2,250 to $2,500	1,254,076	3.18	89.32	2,968,932,000	5.01	62.34
$2,500 to $3,000	1,475,474	3.74	93.06	4,004,774,000	6.76	69.10
$3,000 to $3,500	851,919	2.16	95.22	2,735,487,000	4.62	73.72
$3,500 to $4,000	502,159	1.27	96.49	1,863,384,000	3.14	76.86
$4,000 to $4,500	286,053	.72	97.21	1,202,826,000	2.03	78.89
$4,500 to $5,000	178,138	.45	97.66	841,766,000	1.42	80.31
$5,000 to $7,500	380,266	.96	98.62	2,244,406,000	3.79	84.10
$7,500 to $10,000	215,642	.55	99.17	1,847,820,000	3.12	87.22
$10,000 to $15,000	152,682	.39	99.56	1,746,925,000	2.95	90.17
$15,000 to $20,000	67,923	.17	99.73	1,174,574,000	1.98	92.15
$20,000 to $25,000	39,825	.10	99.83	889,114,000	1.50	93.65
$25,000 to $30,000	25,583	.06	99.89	720,268,000	1.22	94.87
$30,000 to $40,000	17,959	.05	99.94	641,272,000	1.08	95.95
$40,000 to $50,000	8,340	.02	99.96	390,311,000	.66	96.61
$50,000 to $100,000	13,041	.03	99.99	908,485,000	1.53	98.14
$100,000 to $250,000	4,144	.01	100.00	539,006,000	.91	99.05
$250,000 to $500,000	916	(2)		264,498,000	.45	99.50
$500,000 to $1,000,000	240	(2)		134,803,000	.23	99.73
$1,000,000 and over	87	(2)		157,237,000	.27	100.00
All levels	39,458,300	100.00		59,258,628,000	100.00	

[1] From National Resources Committee, Consumer Incomes in the United States (Washington: Government Printing Office, 1938), p. 6.
[2] Less than 0.005 percent.

While such picturizations and comparisons do not of themselves make a complete case for an improvement in the income levels of the poorer laboring groups, they do indicate the existence of a problem which begs for solution. An approach through new, direct legislation would probably not be so useful or productive as a consolidation of gains already made and an emphasis upon a more widespread attitude of trusteeship on the part of management.

[22] A single individual is admittedly different from a family, but a family of 8 or 10 is likewise different from one of 2 or 3. Consequently, when considering income levels it is almost as valid to combine families and single individuals, as we have done here, as to treat them as 2 distinct groups. In such a combination, however, families predominate roughly in the ratio of 3 to 1.

In many respects consumers find themselves in an even weaker position than labor. In reality, of course, a worker is as much a consumer as he is a producer, but the consumer group includes more than labor. It may be useful, therefore, to look separately at the responsibilities and effectiveness of trusteeship as they relate to the consumer-manager relationship.

We have already noted the degree to which managers, rather than consumers acting through the market, have assumed control over prices and obviated competition in a large sector of our economy.[23] The traditional power of the consumer to shop elsewhere if he considers prices too high is now greatly limited or without effect. Under monopoly, it will do him no good to go elsewhere. His remaining choice is to buy or to do without. His power of selection may occasionally be effective if, as one of a group, he drastically limits his purchases when prices are out of line, but results are not nearly so certain as when consumers could abandon an offending merchandiser and buy only from a competitor. So-called consumers' strikes have sometimes been successful for short periods in limited areas, but the history of such efforts does not indicate that they are a potent source of consumer power. Consumers are too diffused and too prone to emphasize their producer rather than their consumer functions. Moreover, many commodities are now considered necessities which must be bought even at high prices. The possibility, therefore, of controlling managers through selective purchasing or through non-purchasing holds little promise.

It should be almost axiomatic that the end of production is consumption, but such a simple proposition has not as yet gained sufficiently widespread acceptance. The same fate has so far met the idea that in a democracy social and economic gains should be mass gains. Rather, it is contended that since improved methods and ideas are the creations of management, the managers and companies should receive the benefits. Without discussing this in detail we should at least point out that it is true only to a strictly limited extent, providing we repudiate the idea of a class society. Second thought clearly reveals that, in general, managers are responsible for only a minor part of each improvement. The new ideas which men have, trace their roots to the ideas of contemporaries and to the contributions of the past. Frequently the fundamental research has been done in university or governmental laboratories or by independent inventors of materials or thought. The product, therefore, belongs not to individuals or even to corporations, but to society as a whole.

If consumption is the end purpose of production, then business policies should be pointed toward the largest possible consumption over a considerable period of time. Prices should be sufficiently high to cover all costs, including that of capital, but should not be substantially above this because of consequent restrictive effects upon consumption. Wages likewise should be adequate to create and maintain a mass market for mass-produced goods. Both investors and executives should be paid enough to elicit their best performance, and there is little reason for paying more.

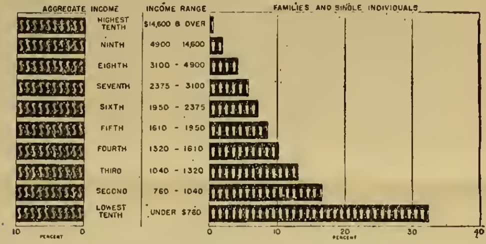
In practice, of course, this ideal of purpose and sharing is imperfectly attained. It is true that each year the consumer is able to

[23] Supra, ch. II.

Chart IX.—Distribution of Income in the United States [1]

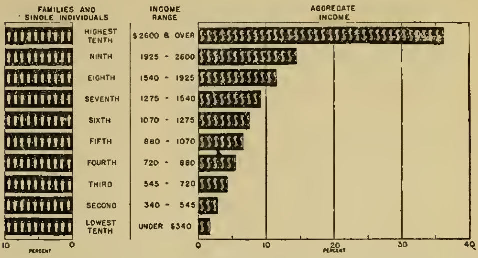
PROPORTION OF NATION'S CONSUMER UNITS RECEIVING EACH TENTH OF AGGREGATE INCOME [2]

1935-36



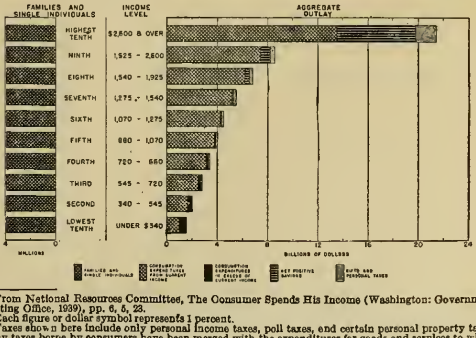
SHARE OF AGGREGATE INCOME RECEIVED BY EACH TENTH OF NATION'S CONSUMER UNITS [2]

1935-36



AGGREGATE OUTLAY OF EACH TENTH OF NATION'S CONSUMER UNITS FOR CONSUMPTION, SAVINGS, AND GIFTS AND PERSONAL TAXES [3]

1935-36



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[1] From National Resources Committee, The Consumer Spends His Income (Washington: Government Printing Office, 1939), pp. 6, 5, 23.

[2] Each figure or dollar symbol represents 1 percent.

[3] Taxes shown here include only personal income taxes, poll taxes, and certain personal property taxes. Many taxes borne by consumers have been merged with the expenditures for goods and services to which they apply. Business taxes and taxes paid on income-producing property were deducted as business expense in calculating the net income of consumers.

buy new products or improved old ones. But what he gets and what he could get are vastly different things. As an executive of one of the largest corporations has stated, "It has always been an internal policy in our company to earn 30 percent on the investment. This will be maintained at all costs. How much we give to labor and to the consumers is a matter of intelligent self-interest." While there is no doubt that the customers of this corporation have progressively obtained increasing value for their money, it is at least an open question whether they could not have received considerably more if competition were more effective. It is not necessary to pay a 30 percent return in order to attract capital to large companies in an established industry.

The administration of the antitrust acts has revealed a number of methods, many of which are now current, whereby trade has been restrained through monopolistic practices to the detriment of the consumer. The emphasis here has been the effect of monopoly on competitors rather than on consumers, but consumers are directly—and usually adversely—affected. Accounts of some of the most famous cases have been given in a number of places.[24] A condensed compilation and discussion of more recent instances has been presented to the Temporary National Economic Committee by the Federal Trade Commission.[25] A perusal of these studies indicates that combination is as natural as competition, and that when competition disappears the consumer is the chief sufferer. It has been observed that—

> it may not accord with reason; but the ordinary executive is prone to look upon a high unit price as the key to profits and is little disposed to experiment with lower prices as a device for securing larger sales.[26]

The preoccupation of businessmen with price raising and price fixing was highlighted by the N. R. A. The power of business here was strong: The governing bodies or code authorities were composed almost exclusively of the businessmen concerned in the particular industries; labor and consumers had scarcely a voice.[27] The codes themselves were drawn up by businessmen and submitted for approval by the N. R. A. For the most part, the wage and employment sections were provisions which the various businesses "were willing to grant 'voluntarily' only in exchange for an increased control over prices, production, and other matters which they regarded as desirable." [28] Indicative of the attitude of mind is the fact that the three most common types of trade-practice requirements written into the codes were: (1) Practices tending to effect minimum price (79 percent of the codes); (2) uniform methods of cost finding (72 percent); (3) open prices (59 percent), usually with a waiting pe-

[24] See, for example, D. M. Keezer and S. May, The Public Control of Business (New York: Harper, 1930); T. C. Blaisdell, The Federal Trade Commission (New York: Columbia University Press, 1932); N. B. Gaskill, The Regulation of Competition (New York: Harper, 1936); and Thurman Arnold, op. cit.

[25] Published as Part 5-A of the Temporary National Economic Committee's series, Investigation of Concentration of Economic Power, entitled Federal Trade Commission Report on Monopolistic Practices in Industries (Washington: Government Printing Office, 1939).

[26] Walton Hamilton and Associates, Price and Price Policies (New York: McGraw-Hill, 1938), p. 548.

[27] L. S. Lyon and others, The National Recovery Administration (Washington: Brookings Institution, 1935), p. 528; Robert H. Connery, The Administration of an N. R. A. Code: A Case Study of the Men's Clothing Industry (Chicago: Public Administration Service, 1938); and the testimony of Lowell B. Mason, former General Counsel for the National Recovery Review Board (The Darrow Committee) in Senate Committee on Finance, 74th Cong., 1st sess., Hearings on Investigation of the N. R. A., vol. 1, p. 1118. Mason's testimony covering pp. 1095–1150 constitutes a sort of summary of the findings of the Darrow Committee.

[28] L. S. Lyon, op. cit., p. 746.

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riod stipulation.[29] In addition, "private price-fixing arrangements * * *, according to competent observers, flourished on a relatively large scale." [30] It was expected that an increase in wages and employment would provide a firm basis of purchasing power for an upturn but price raising and other restrictive practices choked this off. "By the time wages were raised by the codes it was a question of catching up with prices, not of leading them up." [31] That the lesson of N. R. A. was not sufficiently learned was indicated in 1937 when again the hopes of large profits brought about a restrictive rise in prices.

The N. R. A. served as a prominent example of the proposition that particular interests in a narrow sphere are often at variance with the broad public interests. But since businessmen must first of all weigh the effects of policies on their particular concerns, it is natural that they should develop an attitude of mind, a body of preconceptions which causes them to act in ways conducive to their immediate interests rather than to the interests of the economy as a whole.

Thus, the problem now facing consumers and the Nation is the reconciliation of both individual and public interests in big business. Consumers, as we have seen, are weak in this field, for their control is too diffused to be effective. To make up for these deficiencies in their power, therefore, consumers and other groups, including aggrieved businessmen, call upon the Government for assistance.

In a democracy the extent of governmental activity and control is roughly in inverse proportion to the degree to which other agencies satisfy the needs and desires of the people. Prominent businessmen are truthfully arguing that the way to ease governmental interference is for business better to satisfy the needs of the public. Thus the late J. O. McKinsey has said:

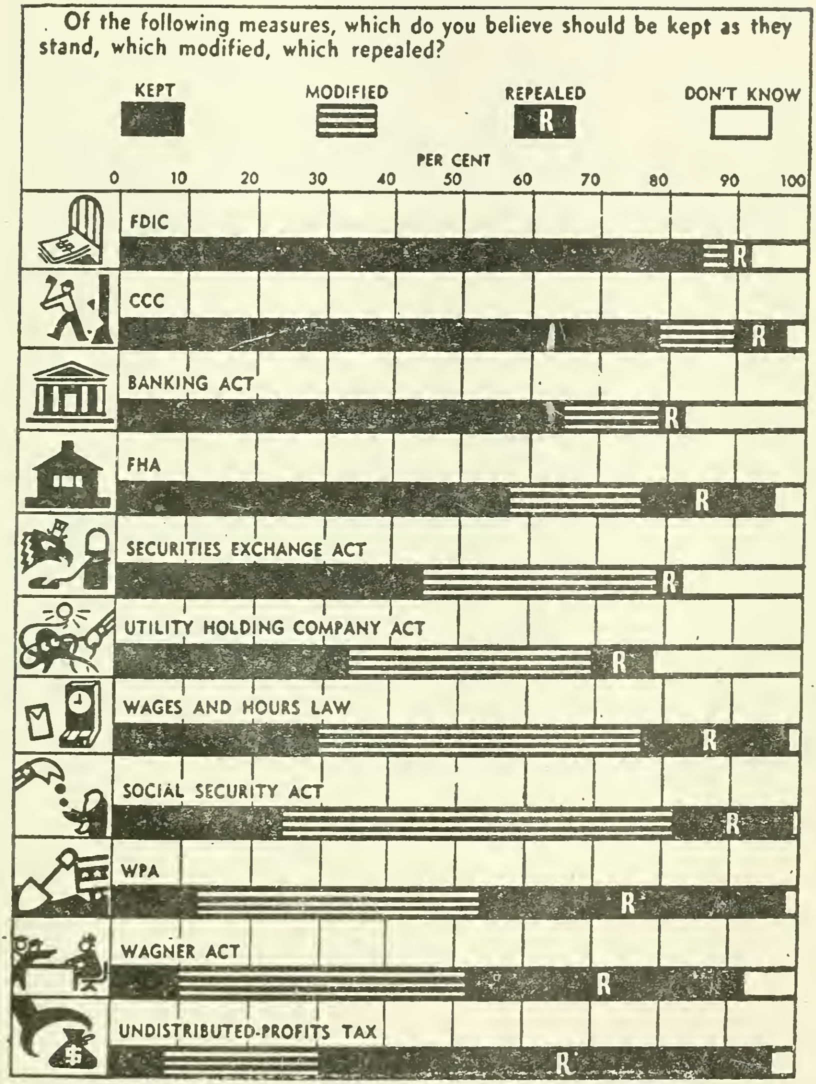
> Specialization and rapidity of economic changes tend to produce maladjustment in our economic organization which leads surely to government interference. Granted the first two conditions, the third follows inevitably. The only effective remedy for this condition is that business may be managed with a greater degree of efficiency so as to alleviate the conditions which make possible the assumption of authority on the part of the Government.[32]

The editors of Fortune magazine contend that a fundamental change in attitude among businessmen has taken place in the last few years. Many executives, they believe, accept and advocate social responsibility.[33] The statements of officials and the recent annual reports of some of the large corporations tend to substantiate this position. It is further bolstered by an opinion poll of businessmen conducted by Fortune on the subject of 11 important items of New Deal legislation which affected business. In only one instance, that of the undistributed-profits tax, was there a preponderance of business opinion for outright repeal, and this action had been taken by Congress before the outcome of the survey was published. A graphic presentation of the results of this poll is given in chart X. The editors comment that—

> With no clear-cut majorities for the elimination from the statute books of the remaining 10, it can be argued that so far as major principles of reform are con-

[29] Ibid., p. 570.
[30] Jules Backman, Government Price Fixing (New York: Pitman, 1938), p. 68.
[31] L. S. Lyon, op. cit., p. 761.
[32] J. O. McKinsey, Organization Problems Under Present Conditions, pp. 8–9.
[33] See "Business and Government," Fortune, XXI (March 1940), pp. 38–39.

CHART X.—OPINIONS OF BUSINESSMEN ON RECENT LEGISLATION [1]



[1] From Fortune, XX (October 1939), p. 53.

cerned, the New Deal has produced nothing that business is not willing to have stand, at least with modifications * * *.

[While] big business, both manufacturing and retail, tends to be more opposed to the New Deal than small business * * * there is a strong inclination to accept as basically good many of the laws business considers need modification. There is a strong inclination, likewise, to suggest modification, rather than repeal, of the laws business considers most baneful.[34]

Perhaps business executives are becoming more professionalized. Perhaps, as John C. Baker suggests—

executives may be assuming functions to society similar to those of doctors, teachers, scientists, and others in professional work. Such men are rewarded in other ways than merely by financial payments. Avarice, it must be remembered, is not the only motivating factor in human life. If the executive group takes on a professional status, payments may be smaller in cash, larger in other satisfactions, greatly simplified, and incidentally, executives may have a more peaceful existence and live longer. One important reason favors such a development. A quarter of a century ago, "business was business"; i. e., businessmen generally strove mainly for profits. Today the social implications of executive work have so changed that no longer can such men think of business chiefly as corporate profits. They must consider their decisions in terms of social well-being as well as in terms of dividends and personal financial reward.[35]

Trusteeship, then, has broad application. To observe its tenets, business executives must consider not only their own immediate interests but also those of the disfranchised owners, the workers, the consumers, and finally, of that agent of the general public, the Government. Heretofore, the managers of large corporations have placed themselves in the most advantageous position. Their behavior toward owners, labor, and consumers is spotty—sometimes favorable; sometimes, as we have seen, quite the reverse. In spite of the change in attitude which may be taking place, there remain nevertheless many deficient portions in the trusteeship pattern. A problem of government, and especially of the Temporary National Economic Committee, is to suggest ways in which the defective parts of the existing structure of trusteeship may be improved without weakening other parts of the economy. To a discussion of some such methods we now turn.

[34] "What Business Thinks," Fortune, XX (October 1939), pp. 52, 90.
[35] John C. Baker, op. cit., p. 254.

CHAPTER XI

SECURING AND ENFORCING TRUSTEESHIP

In seeking to make trusteeship more effective there is no reason for subjecting business and businessmen to more regulation than is clearly necessary. This is particularly true with respect to various formal controls which might be instituted. Under a philosophy of liberal democracy, individual liberty is to be furthered so long as it does not injure the rights and freedom of the majority. Complete liberty would, of course, result in chaos; and in the end no one would be free. Restrictions, therefore, must be established in order to prevent the few from infringing upon the liberties of the many.

In controlling individuals it is likewise necessary, in line with a liberal democratic philosophy, that the methods be as informal as possible. Formal coercion is a last resort, drawn upon only when other devices fail. Similarly, in devising and installing such additional regulation as may be necessary to make trusteeship in big business more effective, drastic measures should be avoided until it is certain that a milder course will not do.

Our examination of the shortcomings of trusteeship indicates that some additional control over management is necessary. Depressions, wastes, losses to stockholders, mistreatment of labor, and discrimination against the consumer should be eliminated so far as possible. To the administrative realist, however, it is apparent that excessive regulation may defeat its own purpose. If managers must take minute account of a multitude of rules, their initiative may fail, authority may be diffused, and the whole administrative machinery slowed down or even stopped. Consequently, from the administrative as well as from the democratic viewpoint, informal or general devices may actually be more effective, all social values considered, than a rigid and complex system of formal regulation. The methods of securing more effective trusteeship which we shall discuss, therefore, will be general and flexible rather than exact and rigid.

Fortunately, gregarious man usually responds as he is expected to. Most men will play the game according to the rules if the rules are known and accepted. Regarding the development of socially responsible business leaders, for example, Wallace B. Donham, dean of the Graduate School of Business at Harvard, has said:

> If the community gets this social point of view, if it rather questions mere money-making, if money-making without social standards is frowned upon and if real social accomplishment is esteemed * * * we shall get the real leaders in a sufficient number, because it is the approval of the tribe that determines the types of leadership exercised by its leaders.[1]

It is usually when trusteeship is not expected of managers that they fail to live up to its tenets. What is urgently needed, therefore, is

[1] Wallace B. Donham, "The Professional Side of Business Training," in Business Management as a Profession, edited by Henry C. Metcalf (Chicago: A. W. Shaw, 1927), ch. XIII, pp. 228-229.

a wider knowledge and acceptance of its requirements, together with the development and application of other techniques whereby it can be made more effective. Much of what we shall discuss, therefore, is pointed toward supplying the various interested groups with information whereby they may judge trusteeship for themselves, as well as toward suggesting certain structural changes which may make management more responsible without unduly infringing upon essential administrative freedom. Because it is commonly supposed that boards of directors are the guardians of the interests of nonmanagement groups—particularly, of course, the owners—and because boards are formally designed[1] for that purpose, our discussion may well begin with them.

An approach through the boards of directors.—The functions which boards of directors perform differ considerably as between theory and practice. The ideal pattern of board activities has been set forth by the late J. O. McKinsey:

1. It should be responsible for establishing the general objectives of the business
2. It should establish the major policies of the business.
3. It should determine the organization structure of the business and select the major executives * * *.
4. It should be responsible for "checking up" on the executives of the business to whom the responsibility for its administration has been delegated.[2]

McKinsey recognized that the board is unavoidably dependent upon the major officers of the company for much of the information necessary to intelligent action, but he nevertheless maintained that it should constitute substantially more than a facade. A former Assistant Secretary of Commerce, among others, also argues convincingly along similar lines.[3]

We have already seen[4] that in practice many boards today are little more than formal ratifying bodies for the decisions of management. In many cases they could be eliminated and almost no one would realize it. Their important functions have been largely removed; a nearly inanimate body remains. However, in the past and in a few current instances, boards have demonstrated that they can be of value in improving administration and making it more sensitive to the demands of interested groups. Hence, rather than merely sorrowing over their demise and looking for a suitable substitute which may be difficult to find, it would be more profitable to revitalize the now decaying institution. Several possibilities are suggested.

First, the present trend toward officer boards should be reversed. The mere fact that executives know more about a particular business than outside directors possibly can is no adequate reason for creating a management board. A director should have a knowledge of the business which he directs, but he does not need to know all of its details. His function is different from that of the executive. He must check on executives, for one thing, and this cannot adequately be done if the executive and the director are the same person. Moreover, the ingrowing tendencies of officer boards must be eliminated if a broad view of corporate policies is to be attained. "There are not enough outsiders on the board," one corporation executive complains. "We

[2] J. O. McKinsey, Functions of Boards of Directors, Board Committees and Officers, p. 4.
[3] See Richard C. Patterson, "Wanted: Directors Who Direct," New York Times Magazine, January 21, 1940, p. 6.
[4] In ch. III.

need more men who are aware of national trends." [5] If trusteeship is to have any broad, effective meaning, men who can see things in perspective are indispensable. The head of one of the Nation's largest concerns maintains, for example, that "officers universally lack perspective."

Stating a need for effective outside representation on the boards of the great corporations and attaining that goal are, unfortunately, two different things. However, it might be of substantial assistance if some governmental body, such as the Temporary National Economic Committee, were to deplore the present tendency toward officer boards and to underline the opinions of corporate officials who feel that the demise of the outside board will ultimately be a serious thing for business. It may not be necessary to enact legislation requiring, say, that no corporation engaged in interstate commerce may have more than two-thirds of its board members composed of present or past officers of the company or its affiliates Less drastic means should first be tried, but the possibilities of such legislation might meanwhile be studied.

In securing outside representation on boards of directors it is not necessary nor even desirable that members be selected specifically to represent special interests. Our observation has been that the members of boards, committees, or commissions who are expressly chosen because of a particular interest, too often represent and defend it to the unfortunate exclusion and possible detriment of others. In selecting directors, therefore, it is clearly advisable to obtain men who have an extensive specialized knowledge together with an ability to see things whole and in relation. Then their attitudes will fit into the total pattern which must be created. Patchwork is no substitute for mosaic in the development of corporate policy.

In addition, there should be a limit to the number of directorships which one person may hold. We have heard of a case where one man was a member of more than 50 boards; obviously he could not be active on any but a few. This type of board member usually serves merely as window dressing for the corporations involved.[6] The subterfuge operates at cross purposes to responsible business trusteeship because people depend on the integrity of those whose names they see in the annual reports, irrespective of the degree of influence they may exercise.

A limitation on the number of directorships which one man may hold would also reduce corporate combinations through interlocking directorates, now one of the methods of achieving various degrees of monopoly.[7] It would also help to insure the safety of stockholder interests which might otherwise occasionally be sacrificed to those of outside, possibly competing companies on whose boards a particular director also serves.

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[5] In a study of boards of directors, E. H. Schell found that in 1928 only 8.8 percent of the directors of 62 large manufacturing companies were chosen primarily because of their knowledge of external business conditions. See his "Trends in the Functions and Composition of Boards of Directors," in Handbook of Business Administration, edited by W. J. Donald (New York: McGraw-Hill, 1931), pp. 401, 405.

[6] Table II, p. 6, indicates the extent to which a few men hold many directorships in a limited number of the largest corporations.

[7] Information of a related nature in possession of the Securities and Exchange Commission would be of material assistance in showing intercorporate combinations and individual influence through stockholdings. To this end it would be valuable to those interested and to the general public if the Commission would issue an annual report similar to its 1936 Official Summary of Holdings of Officers, Directors and Principal Stockholders. Such information should be more currently available than it is at present.

Finally, a limitation on the number of directorships would make it possible for a man really to direct in one or a few companies. Talent and effort can be spread so thin as to be ineffective.

As regards remedies, the public disapproval of multiple directorships may bear some fruit. In addition it might be practicable to require that all corporations engaged in interstate commerce shall apprise their stockholders, in annual reports or requests for proxies, of the number of positions held by each director or nominee, and the names of the companies involved. Stockholders would then realize that many directors contribute their names only and the situation might correct itself. A last resort would be the enactment of legislation to limit the directorships which may be held by one person to two or three, and those in noncompeting concerns.

In the third place the effectiveness of boards might be increased by limiting their size. Of the 20 largest industrial corporations, the 8 largest utilities and the 8 largest railroads in 1939, nearly half had boards with 15 or more directors. On the whole it was the smaller boards which were the more active in corporation affairs. While it is not possible to establish the optimum number of directors in every case, our observation indicates that in general 10 is better than 15, while a group larger than 15 rarely operates successfully as a unit. Although it may be inadvisable to limit the size of boards by legislation, limitation might become a more or less automatic concomitant to the suggestions which we have made as well as to some which follow.

It is not necessary that directors give all of their time in order properly to discharge their functions. Full-time board members tend to divide administration among themselves and so to destroy unity. The board should be a policy and control group, not an administrative body. Managers are chosen for the latter task. If a man held but a limited number of directorships and applied himself in those positions, he could gain an adequate knowledge of the affairs of the companies involved and at the same time develop other interests which would increase his value as a director. The appointment of committees and of staff employees who would gather information for the use of directors would help them in the important decisions which they must make. Such a procedure would be in keeping with American tradition.

If directors are really to direct, they must be appropriately paid. A nominal figure implies that their contributions are equally nominal.

A common director's fee in the larger companies, for example, is $20 a meeting, plus traveling expenses if necessary. With monthly meetings—weekly gatherings are rare—this is an insignificant annual sum [8] for a man who is liberally compensated in his primary position. It is now time to pay directors an amount sufficient to elicit their best efforts.[9] Although it is not feasible to require any given level of remuneration by legislation, it would nevertheless be useful if voices were raised in support of adequate compensation. The Temporary National Economic Committee can be of valuable assistance in this effort.

Finally, stockholders should be given more information about directors. In the annual report or in requests for proxies the directors or nominees should be listed, each with his qualifications, the number of other directorships which he holds and the companies concerned,

[8] Cf. E. H. Schell, op. cit., pp. 408–409.
[9] Cf. R. C. Patterson, op. cit., p. 18.

and his attendance record if he is already on the board. It might even be desirable to require that men may be nominated by the owners of any 10 percent of the voting stock and that the names and qualifications of such men be circulated to the stockholders in advance of the annual meeting. While the management's slate would probably continue to be elected intact, such a procedure might nevertheless compel managers to select qualified men. Even if such a choice were not offered the stockholders, the other information we have mentioned might discourage mere figureheads from accepting offers of directorships, and might also discourage management from making the offers in the first place. There is little valid objection to furnishing this information, but the mere suggestion may be insufficient. The matter could be covered, if necessary, by legislation so far as interstate companies are concerned.

In summary, it must be recognized that directors must be expected to direct if they are to gain the desired degree of influence. In addition, men with outside views and interests should be elected to boards, the number of directorships held by any one man should be limited, boards should be kept workably small, directors should be appropriately remunerated, and owners should be supplied with adequate information about their representatives. Trusteeship has suffered because directors have been remiss in their legitimate duties. Perhaps some of their faults can be corrected through the methods we have indicated.

The use of publicity.—Dennison and Galbraith have aptly commented that "business operations should be brought into the broad daylight and we look upon this, of itself, as a wholesome influence in encouraging what is good and discouraging what is unwholesome in the business world, and thus as reducing the extent to which regulation need go." [10] It is only through a widespread knowledge of business facts that some of the basic assumptions of competitive economic theory have any validity. It is incongruous to argue that a customer, a worker, or an investor is at liberty to direct his talents or his assets into the channels most beneficial to him if he has only a hazy idea as to where or what those channels are. Adequate publicity thus serves as an aid to achieving trusteeship as well as a substitute for more drastic methods of regulation.

When the economic machine becomes stalled or when waste occurs, investors, managers, workers, and consumers all suffer. To the extent that adequate information would help management to act wisely, to direct economic efforts into the best channels, to forestall economic crises by correcting unwise action before it is too late, executives would be in a better position to discharge their obligations as trustees. The information which they require is of several kinds.

First, extensive reports on production and sales, available to everyone interested, would be of assistance to managers in deciding on plant expansions, production plans, and in the development of new markets. Much of the contributions of investors could thus be saved and one apparent cause of depressions removed through the resultant increase in the accuracy of business judgment. Thus, managers could more readily discharge this phase of their duties as trustees.

Information of these types would not destroy management's incentive to develop new methods because trade secrets could be guarded

[10] Dennison and Galbraith, op. cit., p. 119. For fuller treatment of several of the ideas presented in this section the reader is referred to their book.

and the patent system resorted to. Nor does the objection that it gives competitors an unfair advantage carry sufficient weight. While it is true that the rivals of a given company would know more about its affairs than is now the case, it is likewise true that the managers of that company would know more about the affairs of its rivals. The advantages should, on the whole, more than offset the drawbacks, for all would profit through better business judgment.

Publicity on wages and hours for specific companies would be of special value to labor. Monthly or quarterly reports on rates of pay and hours of work for particular groups of employees, and the number employed in each class, would benefit labor in two important ways: It would reveal employment opportunities and it would shine the white light of public knowledge upon the substandard employer. The latter would serve greatly to increase the effectiveness of managerial trusteeship toward labor.

Reports of the types we have mentioned should be blended with those currently sent by business to the Federal Government. The elimination of duplication would go a long way toward gaining better cooperation with business in putting such a program into effect. Moreover, the whole of the information would then be more readily available and useful to interested persons.

A further refinement in this reporting plan is suggested by the present practice of some corporations. In an attempt to decentralize administration, subordinate executives are given substantial freedom to act when the occasion arises without consulting their superiors; or they may be allowed to ignore a given company policy or headquarters recommendation if they feel that they have a better method. However, when an executive acts in line with this freedom he must be ready with his reasons for doing so. In this way freedom is accorded but made responsible. Our observation indicates that the method is usually successful.

This technique might usefully be applied to the reporting system which we have suggested. Our need today is to increase production, consumption, and employment. To this end it might be required that whenever the managers of a company decide to decrease employment or production they present to the Government their reasons for such action when they report the change. The agency to which they report should not have the power to disallow the modifications. It should, however, be able to require additional information when that submitted is inadequate. Such a method of encouraging business responsbility without destroying justifiable freedom of action merits serious consideration. We believe that it might be of substantial assistance in increasing the trusteeship of big business toward the economic needs of the Nation.

A further type of publicity relates to the responsibility of business toward consumers. Without adequate information, consumers are at the mercy of an unscrupulous or careless seller. If they had a better knowledge of quality and if there were a standardization of grades, they would be more intelligent buyers. This in turn would have the effect of encouraging responsible sellers and penalizing the vendors of inferior merchandise. Thus, trusteeship in relation to the consumer would be enhanced.

The Federal Government already has the basic machinery for rating finished products in both the producer and consumer goods fields. The Bureau of Standards tests a wide variety of products, from steel

girders to thermometers. The Department of Agriculture carries on research in connection with the most common items of consumer goods, particularly those quite closely identified with agriculture. With these agencies as a nucleus, it would not be difficult to expand the Government's testing and grading activities. To be really effective, however, the results of all tests should be freely accessible to producers and the general public alike. The vendors of superior goods should not object, while those who ignore their trusteeship duties would be prodded into better performance.

In summary, therefore, publicity directed into the proper channels and given a continuing rather than a sporadic nature would have great value in improving trusteeship without substantially limiting the freedom of initiative so essential to vital administration. In addition to the increased information on directors which is desirable, the light of continuing publicity should be thrown upon production, sales, inventories, prices, wages and hours, and the quality of goods. In this way, managers who are deficient in trusteeship may be stimulated to more acceptable behavior and, at least as important, the well-intentioned managers would be able more intelligently to exercise their business judgment.

Direct responsibility through legislation.—Since managers have in effect assumed a fiduciary position in relation to stockholders, their subjection to a control similar to that of ordinary trustees might be assumed. While it is true that they should be held more responsible than heretofore, however, we do not advise that stricter supervision be immediately extended to the management of the large corporations. There are two reasons for this. First, if the less formal methods which we have recommended are sufficient, there is no point in imposing further regulation. In the second place, an adequate traditional base does not as yet exist on which to erect such a structure. To be effective, laws must have public support based both on need and tradition. The methods which we have suggested fit in with tradition and should be tried first. Later extensions are a matter for later consideration in the light of the then current facts.

Nevertheless, there is at least one justifiable extension of control in addition to those we have recommended, which might be met by State or Federal legislation as regards large interstate corporations. When certified public accountants audit the books of such a concern they should, of course, satisfy themselves they are "in accordance with accepted principles of accounting," but in addition they should sample the accounts to see that they are in themselves correct. The mere appearance of conformity to rather nebulous principles of accounting is not enough.[11]

[11] For example, the accounts of the crude-drug division of McKesson & Robbins were kept in superior shape by F. D. Coster, even though it was here that the removal of millions of dollars of the company's funds was accomplished. See "McKesson & Robbins: Its Fall and Rise," Fortune, XXI (March 1940), p. 72 ff. Moreover, accounting principles are far from settled. Illustrative of this is a study made by H. C. Greer. He analyzed and compared the annual financial statements of 20 industrial enterprises over a period of 8 years. These statements bore the approval of certified public accountants, indicating that the accounts had been kept "in accordance with accepted principles of accounting." In spite of this, he found a "lack of uniformity in the treatment of items and transactions of identical character * * * sufficient to convert losses into profits, to alter materially the values assigned to important assets, and to render the several statements wholly noncomparable except with substantial revisions in the interests of consistency." More specifically, he found that the application over the 8-year period of the most restrictive interpretation of profits used by the companies "would have produced an aggregate net profit for all the companies combined of about $125,000,000, while the most liberal application, if consistently followed, would have produced an aggregate profit of about $275,000,000. It is noteworthy also that none of the differences result from the difficulties of measurement of values (in which accounting judgment is considered so important); they arise exclusively from differing opinions as to what constitutes a profit."—Howard C. Greer, "What Are Accepted Principles of Accounting?" The Accounting Review, XIII (March 1938), pp. 25–31.

There is an obvious remedy for many of the deficiencies of managerial responsibility which has been the subject of considerable discussion. That is the removal of the laxness, conflict, and even competition of State incorporation laws by requiring uniform Federal charters for interstate corporations.[12] There is much to be said for this procedure and it merits more consideration than we may give it here. It should be pointed out in passing, however, that Federal incorporation is not a prerequisite for Federal control over interstate companies. That may be accomplished directly. So the information and other items which we have mentioned may be gained by direct, specific legislation if necessary. This approach, without uniform incorporation, would, moreover, have the effect of regulating by Federal action phases of corporate functions which should be so controlled, while the remainder would properly be left to the States. Such a procedure has not only practical advantages but fits into the American tradition of government as well.

Conclusion.—A widespread, favorable attitude of mind is a first essential to effective trusteeship in big business. People must expect and assume that managers will look out for interests other than their own. Managers in their turn will then attempt to live up to expectations. It is important, therefore, that any additional regulation, whether formal or informal, should be designed to stimulate and preserve this favorable attitude among corporation executives. Management clearly controls the large concerns, and its cooperation is essential to an economy of abundance and fair treatment. Executives must more clearly realize that restriction by individual companies is disastrous when universally practiced. The methods which we have suggested for securing a more effective trusteeship, therefore, are modeled in such a way that the necessary attitudes of both businessmen and the public may at least be maintained and possibly even improved.

The boards of directors of the large corporations may be more effective instruments of trusteeship if they are modified in several ways. The trend toward eliminating outside directors must be reversed, the number of directorships held by any one man should be limited, boards should be kept reasonably small, the directors should be paid more, and more expected of them. Much of this can be accomplished by publicity of various kinds which we have suggested; some may require legislation.

Trusteeship can also be made more effective through publicity on production, sales, wages and hours, and the qualities of goods. The light of day on corporate activities can have naught but a salutary effect. Moreover, if such publicity is continuous instead of sporadic, it will be more effective and at the same time less disruptive to businessmen.

In general, as far as the element of trusteeship is concerned, legislation providing for more direct supervision of business affairs should be kept in reserve until it becomes unmistakably necessary. A cooperative working out of our problems along the lines we have indicated may in the long run be more productive than more drastic action. An economy of abundance is our goal. An improved sense of trusteeship would materially hasten its achievement.

[12] For a comprehensive presentation of proposals on Federal incorporation, see the Federal Trade Commission's Utility Corporations, Pt. 69-A, S. Doc. No. 92, 70th Cong., 1st sess. (1934).

CHAPTER XII

SUMMARY OF FINDINGS AND RECOMMENDATIONS

The giant corporation of today is almost as revolutionary in its social effects as the invention of the steam engine over a century and a half ago. Leaving aside, as we have, the question of limited liability and dealing solely with the obtrusion of bureaucracy and the increasing importance of trusteeship in big business, the evidence to support so sweeping a statement clearly emerges from the preceding pages of this study.

The central problems with which we have dealt are as old as statecraft. What distinctiveness they possess lies in their relatively recent appearance in the business organizations of western European countries, and particularly in those of the United States.

The underlying problem of trusteeship may be simply stated: When power becomes concentrated in the hands of a few persons, can they be influenced to wield their authority in behalf of interested groups, and to restrain a desire to aggrandize themselves through their strategic positions; or, if those groups are to be protected, must formal sanctions be established which possess coercive power?

The age-old question of bureaucracy may also be reduced to simple terms: When any human organization becomes large, hierarchical, professionalized, and operated by formal rules of teamwork, are the resulting losses of individual initiative, freedom to adjust to changed circumstances, dispatch, efficiency, and sensitivity to consumer demands, so inherent in the complex mechanism that they are inevitable and ineradicable; or, on the other hand, can these socially objectionable aspects of large size be eliminated by careful planning and skillful management on the part of those in control?

These are practical problems, but they have far-reaching social consequences. Upon the ultimate answer which careful and reliable research may provide depends the substantiation or disproval of what is perhaps the basic assumption of the free-market, competitive system: namely, that the social advantages of relatively small, competing business organizations result in greater efficiency of management and attention to consumer demands, and that these benefits are passed on to the consumer.

Conversely, it is likewise assumed that monopolistic and semimonopolistic conditions inevitably result in loss of price flexibility and the gradual disappearance of resiliency in managerial outlook; hence, the conclusion that flexibility is so important that competition must, if necessary, be enforced by governmental sanction. If, however, it should prove to be true that the undesirable aspects of bureaucracy can be obviated and that price inflexibilities are not necessarily inevitable, this discovery added to the admitted advantages of large-scale enterprise might conceivably change our whole attitude toward

the type of industrial system which people consider best suited to their collective interests. The obvious question, therefore, is whether the best features of the competitive system can be preserved under conditions of increasingly limited competition.

Our study has not attempted to resolve this central problem of political economy; rather, after an examination of the vast published material in this field, supplemented by our own first-hand investigation of a selected group of large corporations, we have attempted to isolate the principal manifestations of bureaucracy, to find the contributing causes, and to indicate what steps progressive firms have taken to eliminate its undesirable aspects. When the data seemed to support such a conclusion, we have suggested the point at which remedial measures appear useless or of limited effectiveness. For convenience, bureaucracy has been divided into two categories, the first structural, the second personnel.

Among the outstanding structural causes of bureaucracy are the separation of ownership and control in the modern corporation; the gradual retrogression of ownership; the diffusion of authority among parties of interest; a declining effectiveness of representative boards of directors; the necessity of formal rules of management, possessing almost the force of law; institutional lethargy resulting from tradition and organizational resistance; inadequate definition of the scope of authority among the various departments and executives; the difficulty of effective communication throughout a complex hierarchical structure; excessive supervisory loads; and the production of specialists rather than men of broad outlook, with a consequent loss of perspective and statesmanship.

As possible correctives to these structural causes of bureaucracy, we have discussed the desirability of a clear definition of objectives, responsibilities, and authority; the periodic reexamination and correction of administrative methods, which we have included under preventive maintenance; the use of standard practices and improved methods of coordination and control; the development and use of unit measurements of performance; decentralization of operations and authority; and increased attention to public-relations methods which point both inwardly and outwardly.

The executive needs of a corporation are in direct proportion to its size and complexity, and it is not surprising that the demand for top-notch executives exceeds the available supply. In our analysis, therefore, we have dealt with the requirements of executive leadership, the age factor, overspecialization, seniority, and devices producing a high level of morale.

It should be clear that our findings on bureaucracy do not point to the need for additional legislation. We suggest, rather, that the Temporary National Economic Committee invite business to recognize more clearly the causes and cures of bureaucracy, for, strange to say, the problem has not received the attention it deserves in view of the interests which are at stake. This apathy has been reflected in the relative lack of detailed studies. We also suggest the possibility of enlisting the help of the Department of Commerce in increasing the productivity of industry by establishing a unit which would deal with problems of large-scale organization and management.

Nonlegislative factors must also be chiefly relied upon in improving managerial trusteeship. Although education is better than coercion, it must be well thought out and it must be effective. Administrative realists believe that excessive controls may defeat their very purpose, for rigidity secured through complex rules may be less desirable than some of the shortcomings traceable to present freedoms. Thus, not only from the standpoint of democracy, but also from that of practical administration, education in responsibility and self-restraint is to be preferred to fiats of law which place too great a burden upon industry.

This is not to say, however, that concrete proposals and remedies are wanting. First of all, the boards of directors of the large corporations must be made more effective. If present tendencies continue the board will become moribund, due largely to the failure of businessmen to realize the shortcomings of the expert. Corporation after corporation has replaced its layman board with an officer board. They seem to have forgotten that the true function of a board of directors is to be representative, to bring outside viewpoints to the company, to carry back to the several interests and to the public at large a report on stewardship, and to command confidence and respect because of the established abilities and public-spirited attitude of the nonofficer members. We agree with the executive who has complained: "There are not enough outsiders on the board. We need more men who are aware of national trends."

The Temporary National Economic Committee, therefore, would perform a valuable service if it were to emphasize in unmistakable terms the necessity of preserving democratic control and responsible self-government in the business domain. The possibility of requiring nonofficer directors by specific statutory provision should be studied, but we suggest that less drastic means should first be tried. Well-thought-out advice and publicity, for example, might discourage multiple directorships, for, as we have shown, the functions of a lay board-member cannot possibly be served when the number of such positions is high. Large corporations might be required to apprise their stockholders of the number of such offices which their own directors hold, but here also, limiting legislation should be regarded as a last resort. Many boards are too large to be effective, but again a legislative remedy is probably not necessary. Furthermore, if directors are to serve in a vital capacity, the average scale of remuneration should be increased, and we recommend that careful attention be given to ways and means of achieving this desirable result.

Finally, stockholders should be given more information concerning board members than they now receive. This should include a statement of the directors' qualifications, the number of other directorships held, and their attendance at board meetings. It might also be desirable to consider ways of making the nominating preferences of stockholders more effective.

Other types of publicity are also indicated. Continual publicity should be given to production, sales, wages and hours, employment, and the quality of goods. All except the last could be gained through periodic reports required of individual companies. In addition it might be advisable to require that reasons be given for proposed

changes which would have the effect of decreasing economic activity. Publicity on the quality of goods could be obtained by expanding the activities of the Bureau of Standards and appropriate testing sections of the Department of Agriculture and their findings made freely available. Legislation would, of course, be required for such regulation by publicity, but the results would be highly beneficial. On the one hand, managers who are deficient in trusteeship would be spurred to more acceptable behavior and, at least as important, those who are well-intentioned would be able to exercise their business judgment more intelligently.

Other more direct legislation may be indicated. Public accountants, for example, should be required to satisfy themselves not only that books have been kept in accordance with accepted principles but that the accounts are themselves correct. Uniform Federal incorporation merits further examination, but it is not a prerequisite for additional regulation and may even be a practical handicap. In respect to trusteeship, it should be emphasized that any additional legislation providing for more direct supervision of business affairs should be held in reserve until it is clearly necessary. A cooperative solution of our problems along the lines we have indicated may in the long run be the more productive course.

In summary, our suggestions for action to the Temporary National Economic Committee may be listed.

On bureaucracy we suggest—

1. That the committee adequately remind business leaders of the problems of bureaucracy, its elements and causes, and the available remedies.

2. That it examine the possibilities of establishing a unit in the Department of Commerce to study administrative problems and to help business in their solution.

On trusteeship we suggest—

1. That the committee give adequate publicity—

   (*a*) To the requirements of trusteeship in order to help build a strong public expectance of such responsible behavior.

   (*b*) To the need for nonofficers on boards of directors.

   (*c*) To the desirability of limiting the number of directorships which one person may hold.

   (*d*) To the desirability of more adequately paying directors and of expecting them actually to direct.

2. That it recommend legislation which will require—

   (*a*) That corporations engaged in interstate commerce furnish periodically to their stockholders data on their directors, including qualifications, other directorships held, and attendance at board meetings.

   (*b*) That such corporations furnish prompt and complete information to the Federal Government upon production, sales, employment, wages and hours, together with reasons for changes which will materially decrease the level of economic activity; such data to be freely available to all interested persons, both by classifications and by individual companies.

(*c*) That the Bureau of Standards and the consumer activities of the Department of Agriculture be expanded to conduct comprehensive tests on products and to make the results freely available.

(*d*) That public accountants certifying the accounts of such companies not only satisfy themselves that the records have been kept in accordance with accounting principles but also that the accounts themselves appear to be correct.

3. That the committee study the possibilities of legislation to be enacted if the milder forms of regulation which we have suggested prove inadequate, such legislation to require—

(*a*) That some set minimal proportion of the members of boards of corporations engaged in interstate commerce be outside, nonofficer, persons.

(*b*) That no person hold more than a set minimum of directorships.

(*c*) Uniform Federal incorporation of corporations engaged in interstate commerce.

(*d*) That the practical effectiveness of the stockholder privilege of nominating directors be enhanced.

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